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THE EFFECT OF AIRLINE DEREGULATION ON THE RURAL ECONOMY

HEARING

BEFORE THE

SUBCOMMITTEE ON
RURAL ECONOMY AND FAMILY FARMING

OF THE

COMMITTEE ON SMALL BUSINESS
UNITED STATES SENATE

ONE HUNDREDTH CONGRESS

FIRST SESSION

ON

THE EFFECT OF AIRLINE DEREGULATION ON THE RURAL ECONOMY

OCTOBER 28, 1987

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HEARING DATE

October 28, 1987:

Morning session 1

THE EFFECT OF AIRLINE DEREGULATION ON THE RURAL ECONOMY

WEDNESDAY, OCTOBER 28, 1987

U.S. SENATE,
SUBCOMMITTEE ON RURAL ECONOMY
AND FAMILY FARMING,
SENATE SMALL BUSINESS COMMITTEE,
Washington, DC.

The Subcommittee met at 9:30 a.m. in room SR-428A, Russell Senate Office Building, Hon. Max Baucus (Chairman of the Subcommittee) presiding.

STATEMENT OF HON. MAX BAUCUS, A U.S. SENATOR FROM THE STATE OF MONTANA

The CHAIRMAN. The Subcommittee will come to order.

I would like to welcome everyone to today's hearing and thank you for coming. This is the second in a series of hearings that this Subcommittee will hold on the problems facing rural America.

In March of this year, the Subcommittee received testimony concerning major obstacles to economic development in rural America.

A critical factor discussed at that hearing was the inability of many cities and communities to obtain dependable, reasonably priced air service. This situation has developed over the past 10 years since Congress deregulated the airline industry.

For those of us in Congress who voted against deregulation, take little satisfaction in knowing that our dire predictions of rural economic havoc have come true.

The time has come to begin a careful analysis of the effects of deregulation on rural America. My home State of Montana has been hit particularly hard.

Since deregulation, seven Montana cities have lost jet service.

Since deregulation, airfares to and from my State and other States have increased dramatically. In 1978, you could fly from Billings to Washington, DC, for $156. Today the same ticket will set you back $337, a 116 percent increase. Fares to New York, San Francisco, Denver, and Seattle have risen by similar amounts.

Since deregulation, Montana and other western rural States have lost a significant amount of air service. Butte has experienced a 50 percent drop in the number of seats available; Glasgow, a 58 percent drop; Kalispel, a 38 percent reduction; Miles City, down 33 percent.

The statistics go on and on, but the message is clear. Montana and other rural States across the country are being hit hard. The

promise of airline deregulation has become a one-way ticket to economic oblivion.

While the big cities of America get more service, rural States and rural communities get less. While they pay less, Montanans pay more. It does not make sense, and it just is not fair.

There are those in and out of the Government who would claim the rural communities are being protected by the essential air service program. Although this program is indeed essential, the minimum level of service provided is wholly inadequate to enable these communities to prosper.

Even with the Essential Airline Service Program [EAS], businesses and citizens in rural communities are being forced to live with: Flight delays and economic cancellations; reduced or abandoned service; inconvenient scheduling; decreased passenger safety; and higher fares.

While these direct results of airline deregulation need to be thoroughly examined, of greater importance is the indirect damage they inflict on rural economies. They include: Increased costs and inconvenience of doing business; decreased ability to attract capital; decreased ability to attract new businesses and industries; decreased ability to attract Federal investment dollars; decreased tourism opportunities; and overall decrease in the quality of life and standard of living for those who work and live in rural communities.

The purpose of this hearing is to expose the full effect of airline deregulation to public view.

It is not a pretty sight.

"Small town U.S.A." is becoming "forgotten town U.S.A." under airline deregulation. The airlines are not only losing baggage, they are misplacing the heartland of America. This trend must be reversed.

Some may say that the market is in control. Their defense of "alternative modes of transportation" and "adequate" air service provided by the "marketplace" only indicate a total lack of understanding of the importance of high-quality air service and the economic development of less-populated parts of our country.

Those same individuals only look at direct costs and benefits to the companies that own and run the airlines. They do not examine the indirect results of those decisions made in an industry that is an essential part of the economic growth for any city or community.

It is apparent that Congress must once again assume the responsibility of ensuring that rural and small communities do not continue to bear the burdens of airline deregulation.

I am pleased that we will be hearing today from representatives of both business and communities most affected by airline deregulation, and from Government agencies that must begin to assume some of the responsibilities for ensuring that rural America is not abandoned.

I look forward to the testimony that will be presented and I hope that we will be able to begin building a foundation for addressing this critical area.

Our first panel will include three very key persons with very direct experience; first, Mr. Russell Pankey, who is with the Mon-

tana Airport Managers Association of Missoula, MT. I have known Russ for years and he is a very able administrator.

We will also hear from Mr. Dean Schofield, with the South Dakota Department of Transportation, and Mr. Bob Anderson, chairman of the National Committee of Cities and States for Airline Service in St. Paul, MN.

Russ, I will begin with you.

STATEMENT OF RUSSELL R. PANKEY, PRESIDENT, MONTANA AIRPORT MANAGEMENT ASSOCIATION, MISSOULA, MT

Mr. PANKEY. Thank you, Senator Baucus.

We appreciate the opportunity to be able to present some testimony before your Subcommittee this morning. As you said, my name is Russell R. Pankey, and I am employed by the Missoula International Airport Authority as director of airports at Missoula, Mt. I also hold the position of president of the Montana Airport Managers Association and, also, a director of the Northwest Chapter of the American Association of Airport Executives, and also a member of the Airport Operators Council International [AOCI].

I also have had more than 30 years of experience in the aviation industry, working both for a major airline and currently in airport management administration. I have been the director at Missoula International for the past 7 years. Prior to that, I worked several years in the Midwest, working with small communities in the area of airline service, new service for the first time.

I represent an industry in Montana that provides an economic impact for the State of more than $580 million annually. I have attached a brochure to my testimony that was prepared by our State association, showing the impact within the State.

This industry, therefore, obviously cannot be overlooked in the economic planning and future business activities that might affect us all. As you know, aviation is a multi-billion dollar contributor to our Nation's economy.

The National Transportation System would be seriously crippled if, for any reason, all aircraft were suddenly grounded or greatly reduced. New industry would find their operating costs increased tremendously; their markets greatly restricted and their total services drastically reduced.

The major scheduled air carriers service only about 500 of the Nations 12,000 plus airports and landing areas. Here in Montana, for example, the number of airports serviced by these airlines fluctuates according to economic conditions. During 1986, only 7 of our State's 120 public-use airports were served by the major air carriers. Obviously, the commuter airports serviced are in addition to the seven mentioned.

The most important point that I would like to make at this time is the fact that our State has, in the past, and will in the future, produce and originate record numbers of airline passenger boardings. Also, that data is attached to the report. However, with the Airline Deregulation Act of 1978, we have seen some tremendous changes in the airline industry service, and I would like to address some of those concerns at this time and point out to you the importance and seriousness of Montana maintaining its current level of

airline service and the need for improved and additional services, in order that the State may continue to grow. This would apply to any State in the United States.

As you know, Montana is very vital to the Nation's economy, especially in the areas of the timber and lumber industry, gas and mining operations, Butte being the richest hill on Earth, two of the Nation's most beautiful and attractive national parks, namely Glacier and Yellowstone which attract record numbers of tourists and travel related activities.

We also house the headquarters of the U.S. Forest Service Aerial Fire Fighting Depot. That represents the whole northwest area. We are also one of the major States in beef production and have a good American quality of life that we want to see maintained.

I would like to specifically discuss at this time, some of my feelings regarding the effects of airline deregulation on the rural economy or rural America.

First, it is my opinion that major impacts on the rural economy was a result of the Airline Deregulation Act and the government's approval in addition to that, of all of the airline merger requests which, in fact, has had a tremendous further impact upon airline service to small communities throughout America.

As I mentioned earlier in my testimony, I spent several years working for an airline on new route authorizations and service to many small communities throughout the Midwest prior to the act. Much blood, sweat, and tears were put into a lot of those communities in receiving their first scheduled airline service. If you can imagine, the communities' major economic emphasis for future development was based on their airport and their airline service.

Continuing, for example, with the merger of Ozark and TWA, Republic and all of its predecessor airlines, Northwest, Western, and Delta, the bankruptcy of Frontier Airlines, Braniff and Continental were all, in my opinion, the result of deregulation and not necessarily in the best interest of the U.S. citizens.

To look at both sides of the coin, however, we have had record numbers of airline passengers handled by the air carriers this past year with approximately 400 million plus passengers, plus millions of tons of air freight and air express being handled.

However, I must point out that these record numbers of passengers have been generated between the large hub city pairs such as the New York-Washington, the San Francisco-Los Angeles, Chicago-Atlanta, Chicago-New York, and so on, with the reverse generally happening in rural America with less service, with smaller aircraft and higher fares being experienced throughout the rural America.

To be more specific, airline service to Kalispell, Helena, Bozeman and other small cities in Montana have been drastically reduced with less carriers and smaller aircraft.

So, on one hand, airline deregulation has had a positive impact on a large number of people in the big metropolitan cities but has had a negative impact on rural America and may have, in fact, crippled the economic development of a large number of smaller cities throughout the country.

We have experienced other uncontrollable circumstances within our aviation industry because of the controller's strike and the

action of our President in that regard and the lack of sufficient personnel within the FAA to properly regulate as provided by law those areas of the aviation industry dealing with safety, certification, air traffic control and all of the other associated regulation enforcement.

The fare structure as provided for under deregulation has also had a large impact on the aviation industry in rural America because, in fact, we do not enjoy the extreme low fares that the major city pairs have and I feel sometimes we, in fact, subsidize the high density markets with our higher, non-competitive fares. Why is the rural America airline customer treated as a second class citizen with higher fares, less service, smaller aircraft, inconvenient schedules, and the list goes on and on.

I have taken the liberty of providing to you a copy of Missoula Airport master plan and a copy of our airline marketing potential study, and we have very thoroughly studied in these documents several items of importance to our future airline service here at Missoula.

We do, in fact, serve seven counties in western Montana, and two counties in northeastern Idaho and do speak to the future of our area in dealing with the population growth, our overall quality of life, our ability to attract Federal investments, and the cost and convenience of doing business in our area.

As you know, under the Federal Airport Improvement Program [AIP], as expired and as proposed in the new legislation, certain Federal dollars are returned to the aviation community as a result of the 8 percent ticket tax and the entitlement formula which, in our case, returns approximately $6 to the Missoula Airport for every airline passenger boarded.

My point here is, as a result of these numbers, Missoula would receive approximately $800,000 annually for airport improvements and O'Hare Field, for example, will receive the new $16.5 million per year. Therefore, you can see that the costs of airline deregulation, obviously, continues to benefit the large airports that do not necessarily need the funds and show the opposite impact to the small cities.

In a regulated environment, we would be looking at certain guarantees of service and funding, but this is not the case in deregulation. The rich get richer and the poor get poorer.

Last, we would also highly endorse and ask for your support in the continued Essential Airline Service Subsidy Program [EAS], to small communities as a part of our overall new aviation legislation.

I have only briefly touched on some of my areas of concern but would impress upon you the importance and the need for continued good, safe, reliable airline service to rural America if we are going to continue to grow and prosper.

We appreciate your support, Senator.

[The prepared statement of Mr. Pankey follows:]

TESTIMONY OF RUSSELL R. PANKEY, A.A.E

MISSOULA, MONTANA

OCTOBER 28, 1987

RE: HEARING ON THE EFFECT OF AIRLINE DEREGULATION ON THE RURAL ECONOMY

I WOULD LIKE TO TAKE THIS OPPORTUNITY TO THANK THE COMMITTEE FOR INVITING ME TO SPEAK TODAY REGARDING A SUBJECT OF WHICH I HAVE GREAT CONCERNS.

MY NAME IS RUSSELL R. PANKEY AND I AM EMPLOYED BY THE MISSOULA INTERNATIONAL AIRPORT AUTHORITY AS DIRECTOR OF AIRPORTS AT MISSOULA, MONTANA AND I ALSO HOLD THE POSITION OF PRESIDENT OF THE MONTANA AIRPORT MANAGEMENT ASSOCIATION (MAMA) AND I AM ALSO A DIRECTOR OF THE NORTHWEST CHAPTER OF THE AMERICAN ASSOCIATION OF AIRPORT EXECUTIVES (AAAE) AND I AM ALSO A MEMBER OF AND VERY ACTIVE IN THE AIRPORT OPERATORS COUNCIL INTERNATIONAL (AOCI) AND HAVE HELD SEVERAL COMMITTEE POSITIONS WITHIN THAT ORGANIZATION. I HAVE ALSO HAD MORE THAN 30 YEARS OF EXPERIENCE IN THE AVIATION INDUSTRY WORKING BOTH FOR A MAJOR AIRLINE AND CURRENTLY IN AIR-

PORT MANAGEMENT/ADMINISTRATION. I HAVE BEEN THE DIRECTOR OF AIRPORTS FOR THE MISSOULA INTERNATIONAL AIRPORT AUTHORITY FOR THE PAST 7 YEARS AND PRIOR TO THAT, SPENT SEVERAL YEARS IN THE MID-WEST WORKING WITH SMALLER COMMUNITIES IN THE AREAS OF AIRLINE MARKETING, PUBLIC RELATIONS AND NEW AIRLINE SERVICES.

I REPRESENT AN INDUSTRY IN MONTANA THAT PROVIDES AN ECONOMIC IMPACT FOR THE STATE OF MORE THAN $580 MILLION DOLLARS ANNUALLY. (ATTACHED TO MY TESTIMONY IS A COPY OF A STATEWIDE ECONOMIC IMPACT BROCHURE THAT WAS PREPARED IN 1985 BY THE MONTANA AIRPORT MANAGEMENT ASSOCIATION--MAMA.) THIS INDUSTRY, THEREFORE, OBV-IOUSLY CANNOT BE OVERLOOKED IN THE ECONOMIC PLANNING AND FUTURE BUSINESS ACTIVITY THAT MIGHT EFFECT US ALL. AS YOU KNOW, AVIATION IS A MULTI-BILLION DOLLAR CONTRIBUTOR TO OUR NATIONS ECONOMY. THE NATIONAL TRANSPORTATION SYSTEM WOULD BE SERIOUS-LY CRIPPLED IF, FOR ANY REASON, ALL AIRCRAFT HERE SUDDENLY GROUNDED OR GREATLY REDUCED. NEW INDUSTRY WOULD FIND THEIR OPERATING COSTS <u>INCREASED TREMENDOUSLY</u>; THEIR MARKETS <u>GREATLY RESTRICTED</u> AND THEIR TOTAL SERVICES <u>DRASTICALLY REDUCED</u>.

THE MAJOR SCHEDULED AIR CARRIERS SERVICE ONLY ABOUT 500 OF THE NATIONS 12,000+ AIRPORTS AND LANDING AREAS. HERE IN MONTANA, THE NUMBER OF AIRPORTS SERVICED BY THESE AIRLINES FLUCTUATES ACCORD-ING TO ECONOMIC CONDITIONS. DURING 1986 FOR EXAMPLE, ONLY 7 OF OUR STATE'S 120 PUBLIC-USE AIRPORTS WERE SERVED BY THE MAJOR

AIR CARRIERS. OBVIOUSLY, THE COMMUTER AIRPORTS SERVICED ARE IN ADDITION TO THE 7 MENTIONED ABOVE.

THE MOST IMPORTANT POINT THAT I WOULD LIKE TO MAKE AT THIS TIME IS THE FACT THAT OUR STATE HAS, IN THE PAST, AND WILL IN THE FUTURE, PRODUCE AND ORIGINATE RECORD NUMBERS OF AIRLINE PASSENGER BOARDINGS (SEE ATTACHED DATA). HOWEVER, WITH THE AIRLINE DEREGULATION ACT OF 1978, WE HAVE SEEN SOME TREMENDOUS CHANGES IN THE AIRLINE INDUSTRIES SERVICE AND WOULD LIKE TO ADDRESS SOME OF THOSE CONCERNS AT THIS TIME AND POINT OUT TO YOU THE IMPORTANCE AND SERIOUSNESS OF MONTANA MAINTAINING ITS CURRENT LEVEL OF AIRLINE SERVICE AND THE NEED FOR IMPROVED AND ADDITIONAL SERVICES IN ORDER THAT THE STATE MAY CONTINUE TO GROW. AS YOU KNOW, MONTANA IS VERY VITAL TO THE NATIONS ECONOMY, ESPECIALLY IN THE AREAS OF THE TIMBER/LUMBER INDUSTRY, GAS AND MINING OPERATIONS (THE RICHEST HILL ON EARTH IN BUTTE), TWO OF THE NATIONS MOST BEAUTIFUL AND ATTRACTIVE NATIONAL PARKS, NAMELY GLACIER AND YELLOWSTONE WHICH ATTRACT RECORD TOURISTS AND TRAVEL RELATED ACTIVITIES. WE ALSO HOUSE THE HEADQUARTERS OF THE U. S. FOREST SERVICE AERIAL FIRE DEPOT WHICH REPRESENTS THE FIRE FIGHTING CONTINGENT FOR THE WHOLE NORTHWEST. WE ARE ALSO ONE OF THE MAJOR STATES IN BEEF PRODUCTION AND HAVE A GOOD AMERICAN QUALITY OF LIFE THAT WE WANT TO SEE MAINTAINED.

I WOULD LIKE TO SPECIFICALLY DISCUSS, AT THIS TIME, SOME OF MY FEELINGS REGARDING THE EFFECT OF AIRLINE DEREGULATION ON THE RURAL ECONOMY:

A. IT IS MY OPINION THAT MAJOR IMPACTS ON THE RURAL ECONOMY WAS A RESULT OF AIRLINE DEREGULATION AND THE GOVERNMENT'S APPROVAL OF ALL OF THE AIRLINE MERGER REQUESTS WHICH IN FACT HAD A TREMENDOUS EFFECT UPON AIRLINE SERVICE TO SMALL COMMUNITIES THROUGHOUT AMERICA. AS I MENTIONED EARLIER IN MY TESTIMONY, I SPENT SEVERAL YEARS WORKING FOR AN AIRLINE ON NEW ROUTE AUTHORIZATIONS AND SERVICE TO MANY SMALL COMMUNITIES THROUGHOUT THE MID-WEST PRIOR TO THE DEREGULATION ACT AND MUCH BLOOD, SWEAT AND TEARS WAS PUT INTO ALOT OF THOSE COMMUNITIES IN RECEIVING THEIR FIRST SCHEDULED AIRLINE SERVICE. IF YOU CAN IMAGINE, THE COMMUNITIES MAJOR ECONOMIC EMPHASIS FOR FUTURE DEVELOPMENT WAS BASED ON THEIR AIRPORT AND THEIR AIRLINE SERVICE. CONTINUING, FOR EXAMPLE, THE MERGERS OF OZARK AND TWA, REPUBLIC AND NORTHWEST AIRLINES, WESTERN AIRLINES AND DELTA AIR LINES, THE BANKRUPTCY OF FRONTIER AIRLINES, BRANIFF AND CONTINENTAL AIRLINES WERE ALL THE RESULT OF DEREGULATION AND, IN MY OPINION, NOT NECESSARILY IN THE BEST INTEREST OF OUR U.S. CITIZENS.

TO LOOK AT BOTH SIDES OF THE COIN, HOWEVER, WE HAVE HAD RECORD NUMBERS OF AIRLINE PASSENGERS HANDLED BY THE AIR CARRIERS THIS PAST YEAR WITH APPROXIMATELY 500 MILLION PASSENGERS, PLUS, MILLIONS OF TONS OF AIR FREIGHT AND AIR EXPRESS

BEING HANDLED. HOWEVER, THESE RECORD NUMBERS OF PASSENGERS HAVE BEEN GENERATED BETWEEN THE LARGE-HUB CITY PAIRS SUCH AS THE NEW YORK-WASHINGTON, D.C., SAN FRANCISCO-LOS ANGELES, CHICAGOATLANTA, CHICAGO-NEW YORK, ETC. WITH THE REVERSE GENERALLY HAPPENING IN RURAL AMERICA WHERE LESS SERVICE WITH SMALLER AIRCRAFT AND HIGHER FARES IS BEING EXPERIENCED. TO BE MORE SPECIFIC, AIRLINE SERVICE TO KALISPELL, HELENA, BOZEMAN AND OTHER SMALL CITIES IN MONTANA HAVE BEEN DRASTICALLY REDUCED WITH LESS CARRIERS AND SMALLER AIRCRAFT. SO ON THE ONE HAND, AIRLINE DEREGULATION HAS HAD A POSITIVE IMPACT ON A LARGE NUMBER OF PEOPLE IN THE BIG METROPOLITAN CITIES BUT HAS HAD A NEGATIVE EFFECT ON RURAL AMERICA AND MAY HAVE, IN FACT, CRIPPLED THE ECONOMIC DEVELOPMENT AT A LARGE NUMBER OF SMALLER CITIES THROUGHOUT THE COUNTRY.

B. WE HAVE EXPERIENCED OTHER UNCONTROLLABLE CIRCUMSTANCES WITHIN OUR AVIATION INDUSTRY BECAUSE OF THE CONTROLLER'S STRIKE AND THE ACTION OF OUR PRESIDENT IN THAT REGARD AND THE LACK OF SUFFICIENT PERSONNEL WITHIN THE FAA TO PROPERLY REGULATE AS PROVIDED BY LAW THOSE AREAS OF THE AVIATION INDUSTRY DEALING WITH SAFETY, CERTIFICATION, AIR TRAFFIC CONTROL AND ALL OF THE OTHER ASSOCIATED REGULATION ENFORCEMENT.

C. THE FARE STRUCTURE AS PROVIDED FOR UNDER DEREGULATION HAS ALSO HAD A LARGE IMPACT ON THE AVIATION INDUSTRY IN RURAL

AMERICA BECAUSE, IN FACT, WE DO NOT ENJOY THE EXTREME LOW FARES THAT THE MAJOR CITY PAIRS HAVE AND I FEEL SOMETIMES WE, IN FACT, SUBSIDIZE THE HIGH DENSITY MARKETS WITH OUR HIGER NON-COMPETIVE FARES. WHY IS THE RURAL AMERICA AIRLINE CUSTOMER TREATED AS A SECOND-CLASS CITIZEN WITH HIGHER FARES, LESS SERVICE, SMALLER AIRCRAFT, INCONVENIENT SCHEDULES, ETC.????

D. I AM TAKING THE LIBERTY OF PROVIDING TO YOU A COPY OF MISSOULA AIRPORT'S MASTER PLAN AND A COPY OF OUR AIRLINE MARKETING POTENTIAL STUDY AND WE HAVE VERY THOROUGHLY STUDIED IN THESE DOCUMENTS SEVERAL ITEMS OF IMPORTANCE TO OUR FUTURE AIRLINE SERVICE HERE AT MISSOULA. WE DO, IN FACT, SERVE 7 COUNTIES IN WESTERN MONTANA, AND 2 COUNTIES IN NORTHEAST IDAHO AND DO SPEAK TO THE FUTURE OF OUR AREA IN DEALING WITH POPULATION GROWTH, OUR OVERALL QUALITY OF LIFE, OUR ABILITY TO ATTRACT FEDERAL INVESTMENTS AND THE COST AND CONVENIENCE OF DOING BUSINESS IN OUR AREA.

E. AS YOU KNOW, UNDER THE FEDERAL AIRPORT IMPROVEMENT PROGRAM (AIP) AS EXPIRED AND AS PROPOSED IN THE NEW LEGISLATION, CERTAIN FEDERAL DOLLARS ARE RETURNED TO THE AVIATION COMMUNITY AS A RESULT OF THE 8% TICKET TAX AND THE ENTITLEMENT FORMULA WHICH IN OUR CASE, RETURNS APPROXIMATELY $6.00 TO THE MISSOULA AIRPORT FOR EVERY AIRLINE PASSENGER BOARDED. MY POINT HERE IS, AS A RESULT OF THESE NUMBERS, MISSOULA WOULD RECEIVE APPROXIMATELY $800,000 ANNUALLY FOR AIRPORT IMPROVEMENTS AND O'HARE FIELD, FOR EXAMPLE, WILL

RECEIVE $16 MILLION+ PER YEAR. THEREFORE, YOU CAN SEE THAT THE COSTS OF AIRLINE DEREGULATION, OBVIOUSLY, CONTINUES TO BENEFIT THE LARGE AIRPORTS THAT DON'T NECESSARILY NEED THE FUNDS AND SHOWS THE OPPOSITE IMPACT TO SMALL CITIES. IN A REGULATED ENVIRONMENT, WE WOULD BE LOOKING AT CERTAIN GUARANTEES OF SERVICE AND FUNDING AND THIS IS NOT THE CASE WITH DEREGULATION. "THE RICH GET RICHER AND THE POOR GET POORER."

F. WE WOULD ALSO HIGHLY ENDORSE AND ASK FOR YOUR SUPPORT IN THE CONTINUED ESSENTIAL AIRLINE SERVICE SUBSIDY PROGRAM (EAS) TO SMALL COMMUNITIES AS A PART OF OUR OVERALL NEW AVIATION LEGISLATION.

I HAVE ONLY BRIEFLY TOUCHED ON SOME OF MY AREAS OF CONCERN BUT WOULD IMPRESS UPON YOU THE IMPORTANCE AND NEED FOR CONTINUED GOOD, SAFE, RELIABLE AIRLINE SERVICE TO RURAL AMERICA IF WE ARE GOING TO CONTINUE TO GROW AND PROSPER.

YOUR SUPPORT WOULD BE MOST APPRECIATED.

SINCERELY,

Russell R. Pankey

RUSSELL R. PANKEY, A.A.E.
DIRECTOR OF AIRPORTS

The CHAIRMAN. Thank you very much, Russ.
Now I will hear from Mr. Schofield.

STATEMENT OF DEAN SCHOFIELD, DIRECTOR, OFFICE OF PLANNING, SOUTH DAKOTA DEPARTMENT OF TRANSPORTATION

Mr. SCHOFIELD. Thank you, Mr. Chairman.

Mr. Chairman and Members of the Subcommittee, my name is Dean Schofield. I am the director of planning for the South Dakota Department of Transportation. On behalf of Gov. George S. Mickelson and the State of South Dakota, I am pleased to appear before you today and explain why our State believes that a reasonable level of air service must be available in our small cities if we are to foster economic development and diversification in the rural areas of our country.

We in South Dakota commend the Subcommittee for holding these hearings. We believe that, as a general matter, the economic problems of rural America deserve greater attention from Washington. Also, as Congress is presently actively considering legislation to extend and improve the Essential Air Service Program, we think that this hearing, focusing on the problems of air service in rural America under deregulation, is particularly timely.

We have reached our conclusion in large part from our experience under the EAS Program created by the Airline Deregulation Act of 1978 and I want to start today with a few words about the EAS Program.

As you know, Mr. Chairman, the EAS Program, which is currently scheduled to expire next year, ensures that many small cities in our country which would not otherwise receive service in the deregulated environment, do receive some minimal scheduled airline service.

The EAS Program does this through subsidy when necessary. Our State is so rural that even our State capitol, Pierre, is one of the seven EAS points. We know that you, Mr. Chairman, along with Senators Pressler and Senator Daschle of South Dakota, Senator Exon, and many others have made clear that air service to these cities and others throughout rural America should not be terminated.

We fully support those efforts to extend and improve the EAS Program as part of the pending airport reauthorization legislation.

Mr. Chairman, at his point I would like to describe for you an everyday example of the vital importance of decent scheduled air service to the economic health of rural America.

In Brookings, which is a town of 16,000 in eastern South Dakota which we spoke about earlier and a subsidized EAS point, there are morning and evening flights daily to one hub—Minneapolis. The 3M Company has a medical products division in Brookings. According to 3M plant manager Jack Yankovich, scheduled air service to Minneapolis was an important factor in why 3M decided to locate the facility in Brookings.

The number of passengers that 3M flies between Brookings and Minneapolis does not sound very impressive—approximately 20 passengers a week. These numbers do become impressive, however,

when you look at the jobs and the dollars that 3M generates into the Brookings economy—650 jobs and $14 million in payroll.

I do not need to tell you, Mr. Chairman, how important 650 jobs are to South Dakota. We doubt that 3M would have located in Brookings if scheduled air service was not available.

According to the station agent for Mesaba Airlines in Brookings, of all the outbound passengers boarding in Brookings in April 1987, 78.8 percent of those were business people. The circumstances in other South Dakota EAS cities is very similar.

In addition to air passenger service, rural America also needs air freight service to serve the manufacturing facilities located in our cities. They are not large enough to afford large inventories of parts and supplies but need replacement parts fast when machinery breaks down. Air service enables these industries to get the parts that they need in timeframes which allow them to remain efficient and competitive.

Adequate airline service is also very important to the future success of South Dakota's tourism industry, which is a very important source of employment for our State. It is especially significant in the recruitment of regional and national conventions in the State.

South Dakota is working very aggressively to meet the changing needs of its economy. We need to provide jobs in town for people leaving the farm. The effects of the economic crisis on the farm are all too real in our State. In response, our State legislature this year took an extraordinary step of enacting a temporary 1 percent increase in the sales tax, the proceeds of which are reserved solely for funding economic development projects in South Dakota.

Having described how important a reasonable level of air service is to the economic health of our rural State, the questions immediately arise as what the level of service has been and how one can ensure the needed level of air service.

Under deregulation and the present EAS Program, service has sometimes been provided with very small planes, only 5 days a week, and at inconvenient times. In addition, in recent years, South Dakota has experienced nearly continuous major—and usually negative—changes in airline service patterns. I have attached to my statement, a table which lists chronologically the many changes in airline service which our State has seen in recent years.

In addition, small aircraft are not readily accepted by our senior citizens. As Senator Pressler knows, Mr. Chairman, South Dakota is one of the many rural States where population includes an increasingly large proportion of senior citizens. These citizens want and need the air transportation system to visit relatives, and yes, even during the winter to go to the Sunbelt.

In summary, air service in South Dakota has been subject to violent shifts in recent years. Notwithstanding recent improvements compared to before deregulation, both the quality and quantity of air service in our rural areas has declined. This has made it more difficult for South Dakota to pull out of the farm crisis and diversify its economy for the long run by attracting new businesses to the State.

As I appear before you today, our State has no specific recommendations for congressional action concerning rural airline serv-

ice other than the legislation to extend and enhance the EAS Program should be enacted promptly.

However, we are very hopeful that these hearings and other initiatives will lay the groundwork for additional proposals which can advance the economic health of rural America.

We intend to be helpful to you, Senator Pressler, and others on this Subcommittee and throughout the Congress as you work on these issues.

Thank you much for the opportunity to appear before you today. At this time, I would be pleased to respond to any questions that you may have.

[The prepared statement of Mr. Schofield follows:]

Statement of

Dean Schofield
Director, Office of Planning
South Dakota Department of Transportation

Regarding

Air Service and the Rural Economy

Before the

Subcommittee on Rural Economy and Family Farming
Committee on Small Business
United States Senate

Washington, D.C.

October 28, 1987

Mr. Chairman and Members of the Subcommittee:

On behalf of Governor George S. Mickelson and the State of South Dakota, I am pleased to appear before you today to explain why our State believes that a reasonable level of air service must be available in our small cities if we are to foster economic development and diversification in the rural areas of our country.

We in South Dakota commend the Subcommittee for holding these hearings. We believe that, as a general matter, the economic problems of rural America deserve greater attention here in Washington. Also, as the Congress is presently actively considering legislation to extend and improve the Essential Air Service (EAS) program, we think that this hearing, focusing on the problems of air service in rural America under deregulation, is particularly timely.

Our message today is not complicated. It is simply that, if our State's efforts to revitalize and diversify its economy are to succeed, our small cities must receive scheduled air service which is reasonable both in terms of quantity and quality.

We have reached that conclusion in large part from our experience under the EAS program created by the Airline Deregulation Act of 1978 and I want to start today with a few words about the EAS program. As you know, Mr. Chairman, the EAS program, which

is currently scheduled to expire next year, ensures that many small cities in our country which would not otherwise receive service in the deregulated environment do receive minimal scheduled airline service. The EAS program does this through subsidy when necessary. Our State is so rural that even our State Capital, Pierre, is one of our seven EAS points. It is simply a fact that, since deregulation, the EAS program has been needed to ensure that most South Dakotans have access to the nation's air transportation system. Four of our cities -- Brookings, Huron, Mitchell and Yankton -- receive subsidy under the EAS program. According to the United States Department of Transportation's REPORT TO CONGRESS ON SUBSIDIZED AIR SERVICE UNDER THE ESSENTIAL AIR SERVICE PROGRAM dated February 1987, service to these four cities "would probably be discontinued" without an EAS subsidy. Thus, if the EAS Program is terminated, under deregulation South Dakota could well face the stark reality of the end of scheduled air service to these cities.

We know that you, Mr. Chairman, along with Senators Pressler and Daschle of South Dakota, Senator Exon, and many others have made clear that air service to these cities and others throughout rural America should not be terminated. We fully support those efforts to extend and improve the EAS program as part of pending airport reauthorization legislation.

Availability of Air Service Promotes Economic Development

Mr. Chairman, at this point I would like to describe for you some everyday examples of the vital importance of decent scheduled air service to the economic health of rural America.

In Brookings, a town of 16,000 in eastern South Dakota and a subsidized EAS point, there are morning and evening flights daily to one hub -- Minneapolis. The 3M Company has a medical products division in Brookings and, according to 3M plant manager Jack Yankovich, scheduled air service to Minneapolis was an important factor in 3M's decision to locate the facility in Brookings.

The number of passengers that 3M flies between Brookings and Minneapolis does not sound overly impressive -- approximately 20 passengers a week. The numbers are very impressive, however, when you look at the jobs and the dollars that 3M generates into the Brookings economy -- 650 jobs and over $14 million in payroll. I don't need to tell you, Mr. Chairman, how important 650 jobs are to our State. We doubt that 3M would have located in Brookings if scheduled air service was not available.

Nor is it a coincidence that five of the newest industries in Brookings have their corporate headquarters in Minneapolis, the designated hub and the only destination for scheduled flights from Brookings. According to the station agent for Mesaba

Airlines in Brookings, of all the outbound passengers boarding in Brookings in April of 1987, 78.8 percent were business people.

The circumstances in other South Dakota EAS cities are similar.

Huron is a subsidized EAS point in central South Dakota. Mr. William Tucker, President of the Greater Huron Development Corporation, has concluded that continuation of the Essential Air Service program is truly essential to the economic well being of his community. He states "Probably our point is best illustrated by the experience we have had in the past and are currently having with the meat packing industry . . . (which) represents something on the order of 600 jobs and a very large investment. The local airport has been a strategic factor in tying the packing business in Huron to major markets and activities outside our area. It is absolutely essential that we have this air service in order to maintain and attract economic development in our community. Our geographic isolation in the heart of the food production country makes this facility absolutely essential to our economic well being."

Mr. Bill Ross, city manager for the City of Yankton, a subsidized EAS point in southern South Dakota, considers the availability of air service critical to business growth. As part of his job, Mr. Ross hosts virtually every industrial or business

concern considering locating in Yankton. He has told us that nine times out of ten one of the first, if not the first question a prospect asks is about airline service to Yankton.

Mr. Marty Kiousis, President of M-Tron Industries which employs 100 people in Yankton, states that "air service is important to M-Tron in our ability to get our customers and employees to and from our Yankton facility. The renewal of the EAS program is extremely important to us in our business growth because it will allow the community to continue to develop its air service connections and to work on expanding air service connections into additional markets that would allow a greater utilization of the service by our business. The renewal of the program, a thorough review of the routing and scheduling, and an improved local promotional program will allow us to bring more of our customers to Yankton thereby improving our ability to market our products."

Mr. Don Anderson, General Manager of Portec-Kolberg, Inc. which employs 300 people in the same city, has indicated that "Continued air service and in fact the improvement of air service in Yankton is most important to us. With our various facilities and corporate headquarters located in Chicago, air service is a must. The continuation and renewal of the Essential Air Service program for Portec-Kolberg, Inc. of Yankton is important for expansions, like the one we just completed which added 150

persons to our work force and to future expansions which may even add more people."

In addition to air passenger service, rural America also needs air freight service. The manufacturing facilities located in our cities are not large enough to afford large inventories of parts and supplies but need replacement parts fast if machinery breaks down. Air service enables these industries to get the parts they need in time frames which allow them to remain efficient and competitive.

For reasons such as these, many businesses, including some with hundreds of employees, have told the Governor's office that they would not have located in, or expanded in, or stayed in Brookings, Yankton, Mitchell, Huron, or other EAS cities, but for the availability of air service. This is particularly true for companies which choose to base sales staff at their home office, even though these salesmen must go on the road frequently. Without air service, South Dakota cities could not attract or retain those businesses.

While I have been talking about factors affecting the location decisions of individual businesses, we must also remember that these individual decisions help establish trends, particularly in small communities. Once one business comes in, it is more likely that another will come in, and once one leaves,

it becomes more likely that others will go. In short, air service is an important factor in economic trends in small cities. We are convinced that the loss of air service in our small towns would have a disastrous effect on efforts to revive and strengthen the local and State economy.

Adequate airline service is also important to the future success of South Dakota's tourism industry, which is an important source of employment in our State. It is especially significant in the recruitment of regional and national conventions to the State.

Teri Ellis, Director of the Sioux Falls Convention and Visitors Bureau, said "Major airline service is a top factor in our getting the regional and national conventions which bring the most dollars to the city. When site selection committees check us out for a convention, direct flights are their first priority." Julie Jensen, Director of the Rapid City Convention and Visitors Bureau, agreed.

Sioux Falls and Rapid City are moderately sized non-EAS cities. Our State capital, Pierre, on the other hand, does not receive air service at a level which is adequate to promote convention business. "We must be able to offer prospective clients frequent, convenient, reasonably priced flights -- or Pierre will not sell," said Diane Anderson, Director of the

Pierre Convention and Visitors Bureau, noting that current service does not meet the requirements of many conventions.

South Dakota is working aggressively to meet the changing needs of its economy. We need to provide jobs in town for people leaving the farm. The effects of the economic crisis on the farm are all too real in our State. In response, our State legislature this year took the extraordinary step of enacting a temporary one percent increase in the sales tax, the proceeds of which are reserved solely for funding economic development projects.

On both the local and the State levels, South Dakota is working to attract new business and industry to expand its economic base. However, from Governor Mickelson on down we are convinced that we need reasonable air service to succeed. Air service is our vital link to the national and to the global economy. We know that rural America presents many attractions for national and foreign investment and tourism, but only where a reasonable level of air service is available.

Recent Difficulties in South Dakota Air Service

Having described how important a reasonable level of air service is to the economic health of our rural State, the questions immediately arise as to what the level of service has been and how one can ensure the needed level of air service.

Under deregulation and the present EAS program, service has sometimes been provided with very small planes, only five days a week, and at inconvenient times. In addition, in recent years South Dakota has experienced nearly continuous major (and usually negative) change in its airline service patterns. I have attached to my statement a table which lists chronologically the many changes in airline service which our State has seen in recent years.

As reflected in that appendix, airline deregulation did not have a major impact on South Dakota until Republic Airlines filed its notice of intent to terminate service to Brookings, Mitchell, Huron and Yankton on February 11, 1981. Republic did not actually terminate those services until late in 1981, at which time Northern Airlines, which was selected by the CAB to provide service to the cities of Brookings, Huron and Mitchell, commenced service. Northern was basically a "paper" airline. It had no previous experience and did not own any aircraft. This airline provided poor service for less than 90 days. Those communities were then without service for nearly 60 days until service was started by Mesaba Airlines with B-99 aircraft. Those craft were not readily accessible to the handicapped and were unable to carry a full load of passengers with baggage. There were delays in luggage reaching destinations. Those experiences created passenger resistance to commuter-type aircraft.

In addition, small craft tend not to be readily accepted by senior citizens and, as Senator Pressler knows, Mr. Chairman, South Dakota is one of many rural states whose population includes an increasingly large proportion of senior citizens. These citizens want access to the air transportation system to visit their relatives and, during the winter, the Sunbelt. Thus, disappointing levels and quality of air service discourage our senior citizens from taking trips of great personal importance to them.

Additional problems stemmed from the shunting of older aircraft from big city routes to South Dakota service. As a result, South Dakota passengers became more familiar than most with, for example, cabin heaters that did not work. An unduly high number of flights were cancelled due to maintenance needs of these older aircraft. These experiences also contributed to the lack of passenger acceptance of new service. Not surprisingly, enplanement levels went down, making service commercially unviable but for the EAS program -- and possibly creating doubt in the minds of businesses as to the future of air service at many points in our State.

Mesaba Airlines has begun to turn that situation around through its recent deployment of larger, pressurized aircraft which can accommodate passengers and their luggage on the same flight. This craft has much better passenger acceptance. Traffic, though still below levels from years ago, is beginning

to increase at points served by this craft and should continue to do so. Mesaba has chosen to use this larger craft on its own, however. Its use is not guaranteed by the EAS program. We think this shows that reasonable equipment must be deployed to put communities on the path to self-sustaining, reliable air service which will make them attractive to business.

Thus, we believe that it has been an exercise in false economy for the Federal government to ensure service to small communities under the EAS program, but provide it at a low level which erodes rather than builds passenger acceptance. We believe that low level service deters businesses from locating in our State. However, the enhanced service requirements which pending EAS extension legislation would provide would greatly enhance passenger acceptance and make our small cities more attractive to business.

Summary and Conclusion

In summary, air service in South Dakota has been subject to violent shifts in recent years. Notwithstanding recent improvements, compared to before deregulation, both the quality and quantity of air service in our rural areas has declined. This has made it more difficult for South Dakota to pull out of the farm crisis and diversify its economy for the long run by attracting new businesses to the State.

As I appear before you today, our State has no specific recommendations for Congressional action concerning rural airline service other than that legislation to extend and enhance the EAS program should be enacted promptly. However, we are hopeful that these hearings and other initiatives will lay the groundwork for additional proposals which can advance the economic health of rural America. We intend to be helpful to you, Senator Pressler, and others on this Committee and throughout the Congress as you work on these issues.

Thank you for the opportunity to appear before you today. At this time I'd be pleased to respond to any questions the Subcommittee may have.

* * * * *

SOUTH DAKOTA AIRLINE ACTIVITIES

07-01-79	North Central merged with Southern Airlines and changed name to Republic Airlines.
10-01-80	Republic acquires Hughes Airwest Airlines.
01-15-81	Republic suspended service between North and South Dakota (11 flights).
02-11-81	Republic filed notice of intent to terminate service to Brookings, Huron, Mitchell and Yankton.
04-10-81	CAB requested proposals from airlines interested in serving Brookings, Huron, Mitchell and Yantkon.
07-07-81	Republic Airlines filed notice of intent to terminate all service to Pierre.
07-31-81	Western filed notice to suspend all service to Pierre.
08-03-81	Air Traffic Controllers went on strike.
08-01-81	Western terminated all service to Piere. CAB ordered Western to resume service to Pierre and continue service until relieved by a designted replacement carrier.
10-01-81	Frontier Airlines began service between Sioux Falls-Denver.
10-05-81	Republic terminated all service to Pierre.
11-11-81	Northern Airlines began service to Sioux Falls-Pierre-Huron-Brookings-Mitchell.
11-18-81	CAB issued Essential Air Service Determination for Pierre.
11-19-81	CAB released Republic from service to Huron-Brookings-Mitchell.
11-22-81	Republic's last service to Brookings, Huron, Mitchell.
11-24-81	Western permitted to suspend service between Pierre-Minneapolis.
12-01-81	Western suspended non-stop service between Sioux Falls-Denver.
12-01-81	CAB designated AAA Airline to replace Republic in Yankton, Norfolk and Omaha market.
02-04-82	Northern Airlines suspended service to Brookings, Huron, Mitchell, Sioux Falls and Pierre.
03-15-82	Republic suspended service from Aberdeen to Rapid City.

04-01-82	Mesaba Airlines started service at Brookings, Huron and Mitchell.
04-25-82	Western dropped service to Denver from South Dakota and changed hub from Denver to Salt Lake City.
04-30-82	Republic suspended service at Yankton.
05-01-82	AAA Air Enterprises began service at Yankton.
05-13-82	Braniff discontinued service.
06-15-82	Permanent selection of Mesaba to serve Brookings, Huron and Mitchell.
07- -82	Texas International began serving Rapid City.
08,09,10-82	Western cut rate fares increased traffic at Pierre with Minneapolis customers flying to Pierre, laying over and flying back to Minneapolis to qualify for a $100 ticket to Hawaii.
09-08-82	United Airlines began serving Sioux Falls.
11-01-82	Continental and Texas International merged.
12-15-82	Republic added an additional flight at Aberdeen and Watertown.
01-26-83	Meeting in Watertown with Republic Airlines resulted in fare revisions which caused traffic to pick up.
02-01-83	Western "I-90 Fares" reduced ticket prices from $208 to $49 round trip from Pierre to Sioux Falls and from $174 to $49 round trip from Pierre to Rapid City.
05-01-83	AAA began serving Sioux Falls from Yankton.
10-01-83	Continental suspended service to Rapid City.
10-01-83	Pioneer began serving Pierre and Rapid City from Denver.
10-30-83	Republic Airlines suspended Aberdeen-Sioux Falls service.
11-14-83	Republic put a DC-9 on Minneapolis-Watertown-Aberdeen-Rapid City flight.
12-05-83	Big Sky began Rapid City-Billings service.
12-15-83	Mesaba Airlines began service from Minneapolis to Sioux Falls and Pierre.
01-04-84	United Airlines began service to Rapid City with 727 Aircraft with two flights a day to Denver.
02-01-84	Republic began Sioux Falls to Rapid City service and eliminated its flights to Sioux City and Kansas City.

J2-01-84	Republic suspended service to Rapid City from Aberdeen and Watertown.
03-12-84	Frontier Commuter plans to begin service from Denver to Pierre and Aberdeen with Convair 580 aircraft.
03-31-84	Pioneer discontinued service to Pierre and Rapid City.
07-02-84	American Central began service in Sioux Falls.
08-15-84	Mesaba Airlines began service in Rapid City.
09-15-84	Big Sky discontinued service in Rapid City.
10-28-84	Frontier Commuter discontinued service to Pierre and Aberdeen.
10-24-84	Western Airlines discontinued service to Pierre.
01-07-85	Northern Airways began service at Aberdeen and Sioux Falls.
02-15-85	AAA discontinued service to Sioux Falls.
07-01-85	Northern Airways discontinued service to Aberdeen and Sioux Falls.
07- -85	American Central discontinued service to Sioux Falls.
12-15-85	Republic Airlines discontinued service to Aberdeen and Watertown.
12-15-85	Mesaba Airlines began service to Aberdeen.
02-01-86	Pioneer Airlines began service to Pierre.
04-01-86	Pioneer Airlines began service to Aberdeen.
04-18-86	Republic Express began service at Sioux Falls.
05-18-86	Pioneer Airlines discontinued service to Pierre, Aberdeen and Rapid City.
05-28-86	Trans-Colorado Airlines began service to Pierre and Rapid City and then suspended service on 08-22-86 to allow them to restart as Continental Express.
07-15-86	Continental Express began service in Pierre and Rapid City.
08-24-86	Frontier Airlines suspended service to Sioux Falls and Rapid City indefinately.
09-30-86	Republic Express discontinued service to Aberdeen, Watertown and Sioux Falls.
10-01-86	Northwest Orient merged with Republic Airlines and now operates as Northwest Orient Airlines in Sioux Falls and Rapid City.

09-30-86	Hesebe Airlines discontinued service to Rapid City.
10-01-86	Hesebe Airlines began service in Watertown.
10-26-86	TransWorld Airlines (TWA) merged with Ozark Airlines and now operates as TWA in Sioux Falls.
11-06-86	Continental Airlines began service in Sioux Falls and Rapid City (original Frontier markets).
11-20-86	AAA Air Enterprises (serving Yankton) name change to Midcontinent Airlines this date.
12-11-86	Delta Airlines' acquisition of Western Airlines approved by USDOT.
04-01-87	Western Airlines name changed to Delta Airlines this date.
04-24-87	Trans-Colorado Airlines operating under the name of Continental Express gave notice of intent to terminate service to Pierre effective May 31, 1987.
05-04-87	Braniff Express began service to Yankton through a contractural agreement with Midcontinent Airlines.
05-14-87	Trans-Colorado Airlines operating under the name of Continental Express discontinued service to Pierre and Rapid City.
05-18-87	Rocky Mountain Airways operating under the name of Continental Express began service to Pierre and Rapid City.
05-05-87	Aspen Airways operating under the name of United Express began service to Rapid City.

The CHAIRMAN. Thank you very much, Mr. Schofield.

I will ask questions when the panel has finished its testimony. Mr. Anderson, why don't you wrap it up.

STATEMENT OF ROBERT W. ANDERSON, CHAIRMAN, NATIONAL COMMITTEE OF CITIES AND STATES FOR AIRLINE SERVICE

Mr. ANDERSON. Thank you, Chairman Baucus.

I thank you for the opportunity to appear before this Subcommittee on this most important subject. I am Robert W. Anderson, chairman of the National Committee of Cities and States for Airline Service. I am the former Mayor of International Falls, MN, and presently the chairman of the International Falls-Koochiching County Airport Commission.

Mr. Chairman, the National Committee of Cities and States for Airline Service was organized to seek the continuation of the essential Air Service Program. Cities and States from West Virginia to Alaska are equally concerned about their economy that their airports serve in those areas.

Good airline service is an economic development tool for all communities. Let me tell you that deregulation has not been kind to our economic well-being in rural America. In my own community of International Falls, where few persons want to visit in the winter because of reported cooler temperatures, the summer is another matter. We have seen the type of aircraft go from the DC–9 jet service that you spoke of in your opening remarks, to Convair 580's. Now, we are presently served with 30 passenger Saabs and 18 passenger Jet Streams. The DC–9's may have been a little bit too much to ask for, however, it is our contention that the aircraft manufacturing industry was not ready for the airline deregulation.

The Convairs are an excellent 48 passenger aircraft with great baggage and freight handling ability. They have the dimensions in their baggage hold to carry good-sized freight, and they have the lift capacity. However, they are getting old.

The Saab 340 is a Swedish made aircraft, that is now serving our community, and while this may be fine for the happy wanderers of Europe with a knapsack on their back, they do not have it when it comes to the American tourist with the two bags that they carry with them. It just does not measure up as an aircraft for Americans.

This is especially true with the fisherman with a grip, a fishing rod, and tackle box. We have the good fortune of being the home of the Voyagers National Park, a large water park in northern Minnesota. Friends, you have not lived until you have seen a group of fisherman at the International Falls Airport with high anticipation to head out to go fishing, with transportation waiting and all ready to go to that wilderness lodge, and their tackle boxes are sitting back at the ramp at Minneapolis/St. Paul Airport. I can tell you that that is not a happy lot.

Let me give you another example about the local fish processor that works all night fileting fish, packing it fresh in crates to ship it to Chicago for a banquet the next evening only to have those crates left in the hot sun on the ramp because there was no room in the plane for that freight. Or, the time that his crates got lost

never to be found again, as he was shipping to a restaurant outside the State. I can tell you after a day or two, somebody is going to know where those fish are because their nose will tell them.

What really happens to that small entrepreneur whose reputation for excellence is lost in situations like that? I can tell you, they are going to take those fish that they catch fresh every day and are going to put them in a refrigerated truck and they are going to haul them to the Twin Cities, process them there and put them on a large air carrier so that they can be sure that they are going to get to their customer. Along with the fish go the jobs from rural America.

Then there is the Camp Koochiching, a place where young boys from around the world come to our area to learn the ways of the woods only to find out that nature is more predictable than whether their luggage will arrive or not, and that they might have to spend the first couple of nights in camp without a sleeping bag.

Some of their parents have gotten wise and are sending their trunks or luggage by way of UPS or by way of freight lines. Well, the airlines want you and your money, but they do not want your baggage or your freight. I could tell you stories and give you examples here until this day turns into night. However, allow me just 1 more minute to tell you about another component to this equation.

In Duluth, MN, boardings have dropped from 139,000 down to 74,000 since deregulation took effect. John Grinden is the airport manager there, and he stated to me that there is only one thing that has caused the passengers to hit the highways, and that is higher fares. You have heard about those already this morning.

The cities in Minnesota had a love affair with the carrier that previously served them for many years, that being Republic Airlines, because we grew up together. And yes, they had a monopoly in many of our cities but not like the one that Northwest has today with the attitude and the fares to match it.

For Duluth there has been some promise of relief because Northwest has come through with some new fares in the past 10 days. So, the jury is still out for the moment but that is just for Duluth. In Rochester, MN, the home of the Mayo Clinic the administrator of the clinic, Mark Bratass, is also on the board of directors for Ozark Airlines. He was quoted in the September 12 issue of the *Rochester Bulletin* this year wherein he stated, "In 1977, 350,000 passengers used the Rochester Airport with 36 flights a day. This year, there will be 260,000 passengers on 18 flights a day. At the end of this week, on November 1, 1987, the daily flights will be cut down to 12 per day, from 36 and now down to 12."

According to Mr. Bratass, who certainly knows the airline industry, it is a Catch-22 situation. He has stated that we will not get better service until we use the Rochester Airport, and we will not use the Rochester Airport until we get better service. So this spiral downward continues.

In closing, I must state that the impact of the airline deregulation in terms of its effect on business, the rural economy and the quality of life is very difficult for us to quantify other than in examples and stories that we can tell you because there has not been studies made.

It is kind of like the long-term disease; it gets progressively worse and you do not realize that you have it until one morning an area wakes up and finds itself that it has lost its attractiveness as a place to do business, to live and to work, and that it can no longer compete. Then its chief export becomes its young people that go off to the big city each day.

Have we been hurt in rural America? You bet we have. Have we given up? Heavens, no. It is bills like this, S. 1752, that give us the hope because of studying an issue that may possibly have some solution that is going to keep us going.

We must have a strong rural economy if we are not all to live in metropolitan America. We must make it possible for the farmers, the woodsmen, the miners, and the fishermen, who are part of the backbone of this country to do business in rural America.

We in the National Committee of Cities and States for Airline Service are not calling for a return to regulation. However, a study that could help educate or enlighten the airplane manufacturers, the airlines, the passengers and the communities would be most helpful.

You can count on us to help where we can, as we strongly this bill of S. 1752, which you have introduced. Thank you for your consideration.

[The prepared statement of Mr. Anderson follows:]

TESTIMONY OF ROBERT W. ANDERSON, CHAIRMAN
NATIONAL COMMITTEE OF CITIES AND STATES FOR AIRLINE SERVICE
BEFORE THE
SENATE COMMITTEE ON SMALL BUSINESS:
SUBCOMMITTEE ON THE RURAL ECONOMY AND THE FAMILY FARM
OCTOBER 28, 1987

Chairman Baucus and Subcommittee Members:

Thank you for inviting me to appear before this important committee which is examining the effects of airline deregulation on the underpinning of the national economic fabric - small business and the rural economy. If we, as a nation, are going to have a strong and vital economy, then we must take measures to foster and develop these national assets.

My name is Robert W. Anderson, Chairman of the National Committee of Cities and States for Airline Service (NCCSAS), which is a national organization formed in Denver, CO, in the fall of 1986. Its purpose is to have Congress enact a new Small Community Air Service Program which would allow cities to develop their potential for supporting a reasonable level of scheduled air service.

The organization has members from Alaska to West Virginia. Many of its member cities and states appeared and testified as to the need for this new program before the House and

Senate Aviation Subcommittees. Support for this program would not have been so broad if it were not so important to small and medium-sized cities.

I am also a former mayor of International Falls, MN, and the current Chairman of the International Falls-Koochiching County Airport Commission. It is from these vantage points that I am commenting to you today.

In your invitation you asked that I address "the effects of deregulation on the rural economy." There are no studies, to the best of my knowledge, that have quantified these effects in terms of business lost, tourism, etc. In fact, the effects are, in most cases, difficult to quantify because they are insidious, like the rot that creeps into wood. One day the wood deck of your house looks sound, the next day a plank breaks under a guest's foot. Upon inspection you find that the plank's interior was filled with wood rot.

In my city, International Falls, MN, which each of you have heard about on the national news due to our unique winter weather, is a city that is dependent upon transportation. In International Falls we must rely upon scheduled air transportation or the private automobile. The passenger bus service is inadquate and the last time a passenger train came to town, it had to back in. We are at

the end of the line for highways and roads which end in wilderness of Minnesota's Arrowhead Region.

As a former mayor of International Falls and the current Chairman of the International Falls-Koochiching County Airport Commission, I have had first-hand experience with the impact of airline deregulation and its effect upon my area. The area's economy is based on wood and paper products, and tourism. It is also a cold-weather, test site for many products that are distributed both nationally and internationally.

In the years prior to airline deregulation, North Central Airlines served the city with 44-passenger Convair 580s and DC-9 Jet aircraft. The DC-9s would be added to the summer schedule to accommodate the influx of tourists, fishermen and hunters who used the city as a jumping off point for wilderness excursions into the surrounding area and Canada.

Deregulation, the stimulus for change in the airline industry, has resulted in dramatic changes in the quality of scheduled air service throughout the airline system. It has had serious impacts in the small- and medium-sized cities. For example, after the merger of Northwest and Republic Airlines, NWA phased out the Convair 580 aircraft at cities like International Falls. It then turned that service over to a surrogate carrier and in the case of my city, the new

carrier uses 30-passenger Saab 340 aircraft.

Since that transition, the city has consistently had problems with air freight and baggage due to the type of equipment the carrier uses. International Falls traffic consists of passengers with alot of baggage - fishing and hunting equipment, dogs, camping gear, etc. It is not the typical "brief case" traffic like you would find traveling in the metropolitan areas.

Mr. Chairman and committee members, you have not lived until you have faced a group of fishermen, full of anticipation, headed for a wilderness lake and their transportation to that lake is setting on the ramp ready to depart, and they have just found out their fishing tackle is back in Minneapolis/Saint Paul simply because there was "no room on the airliner." This is a small matter in the national scheme of things and to some a minor irritation. However, in International Falls and cities like it, it is big business. If our clientele decides that it is too inconvenient to travel to our area and they decide to go elsewhere, we suffer financially because for many people in our area it is their livelihood!

The small replacement air carriers do not utilize the type of equipment that can accommodate passengers, baggage and freight, and in some situations, baggage and freight are

traded for passengers. When this occurs, it creates problems for both the direct and indirect users of the scheduled air service. For example, hunters and fishermen want to have their fish and game shipped to their homes within a reasonable time. One of our local business's, a fish and game processor, which employees 8 or 10 people, has problems shipping the frozen fish and game out of the Falls by scheduled air carrier due to the capacity of the aircraft. These products are highly perishable and they must be kept frozen until they reach their destination.

We have met with the air carrier's management to discuss this and other air service problems, all of which they tend to discount as being nothing more than an inconvenience.

International Falls does not have passenger rail service, and the passenger bus service is not a viable mode of transportation for the business travelers. It's a three hour drive in an automobile to the nearest air carrier-served airport. In winter it can take alot longer. Boise Cascade, who has a paper and wood products operation in International Falls, would have a difficult time in getting personnel in and out of their plant without reliable scheduled public transportation. Most of these travelers are customers, incoming salespersons, technicians and management personnel from all over the nation.

Air Fares are out of sight in our market. The round trip coach fare between Washington, DC and Minneapolis/Saint Paul is $500 or $.27 per mile. To make the 508 mile round trip between International Falls, MN, and Minneapolis/Saint Paul it cost $428 coach or $.86 per mile. On a per mile basis it cost three times more per mile to make the short haul round trip in this market than it does between the larger cities. Of course there is a standby fare between International Falls and Minneapolis/Saint Paul; however, if you need to be somewhere, it does not work too well. This situation is not unique to International Falls. All small- and medium-sized cities have the same problem.

I believe, as a business person, that I understand about market size and market share; however, it appears that the shorthaul fare structure reflects the strategy of the major airlines and their surrogates to control longhaul traffic. Lower fares in the shorthaul markets provides the passengers with an opportunity to switch to a different major airline at the hub airport. In my opinion there needs to be an investigation of airline marketing practices in the shorthaul markets.

Since airline deregulation passenger enplanements have dropped 54 percent nationally, from 1978 to 1985, at cities served by the essential air service program, while passenger enplanements systemwide have increased by 39 percent.

Nothing but poor quality air service can explain this radical difference.

In March, 1987, an Economic Impact Study of the Brainerd-Crow Wing County Airport, located in north central Minnesota, serving a city of 11,488 population, was completed. The study estimated that the direct impact of scheduled air service on the Brainerd area was in excess of $15.0 million annually. During the course of the study employers in the Brainerd area were surveyed and it was found that these businesses employed 4,283 persons, roughly 7% or 303 of these jobs were due to availability of scheduled air service. The annual payroll for these jobs was estimated at $5.9 million.

The study stated that "discontinuance of scheduled air carrier service would affect travel for 43% of the passengers and 32% of the passengers stated that it would affect their business." One in four of the scheduled airline passengers stated that they "would not make the trip if scheduled air service were to be cancelled."

Granted that these data may be hard to quantify, however, when the airport was closed for remarking the airport commission failed to notify area business. As a result the commission received written complaints from neighboring communities and one major area resort indicated that they

faced a possible $300,000 loss in convention business.

Duluth, MN, enplaned 139,000 passengers in 1979. By 1982, passenger enplanements were down 46% to 74,700. Why? John Grinden, Director of the Duluth Airport, says, "high air fares." What happened to these passengers? According to Mr. Grinden, "they were diverted to the highway due to the high short haul air fares to the hub airport."

This diversion of short haul traffic to the highway causes financial problems for airport owners and operators. Revenue at airports is generated on the basis of landing fees, fuel sales, restaurant and other facilities. These revenues are used to meet the airport operating expenses. In the case of the Duluth Airport, if these revenues are curtailed, then the operating expenses must come from other sources. Another financial hardship is created when the air carrier aircraft are downsized. For example, Duluth's terminal facilities are designed to handle jets and large multi-engined aircraft. If the airline serving the city downsizes its aircraft, then these terminal facilities must be redesigned at a huge expense to local, state and federal governments.

Rochester, MN, population 57,800, home of the famed Mayo Clinic, has been seriously impacted by airline deregulation. The Rochester Post-Bulletin, September 12, 1987, carried an

article by Mark G. Brataas, a Mayo Clinic Administrator, on the Board of Directors for Ozark Holding, Inc., in which he states "In 1977, before deregulation, 350,000 passengers used Rochester Airport and there were 36 flights a day - 18 arrivals and 18 departures. This year, 260,000 will use the airport with only 18 flights - 9 arrivals and 9 departures." As of November 1, 1987, the daily flights in and out of Rochester will be cut to 6 each way.

According to Mr. Brataas it is a "catch 22 situation. We will not get better service until we use the Rochester Airport, and we will not use the Rochester Airport until we get better service."

In closing, I must state that the impact of airline deregulation in terms of its effect on business, the rural economy and the quality of life is difficult to quantify. It is an insidious thing. One morning an area wakes up and finds it has lost its attractiveness as a place to do business, to live and to work and it cannot compete, simply because the playing field has been tilted. Its chief export is its young people on the way to the big city.

Mr. Chairman and committee members, this situation needs to be carefully studied so that a determination can be made as to what should be done. We need to have financially sound small- and medium-sized cities and a strong rural economy.

I support S. 1752 which would establish a commission to look into these problems.

The CHAIRMAN. Thank you very much, Mr. Anderson.

I know that Senator Dixon is here, a very able Member of the Subcommittee. Do you have a statement?

Senator DIXON. I wish to put my statement in the record, Mr. Chairman. Thank you. I wish to thank Mr. Anderson for his fine testimony.

[The prepared statements of Senators Dixon, D'Amato, and Kasten follow:]

OCTOBER 28, 1987

STATEMENT BY

SENATOR ALAN J. DIXON

COMMITTEE ON SMALL BUSINESS

SUBCOMMITTEE ON THE RURAL ECONOMY AND FAMILY FARMING

EFFECT OF DEREGULATION ON THE RURAL ECONOMY

Thank you, Mr. Chairman.

Deregulation was undertaken in an attempt to open the airline market to greater competition. It was hoped that this would cause the industry to grow through lower ticket prices and an increase in airline useage. Recently released Civil Aeronautics Board statistics profile the industry change since 1978. The number of airlines tripled in the first five years following deregulation but then declined by 24 percent. The number of passengers has steadily increased to almost double the 1978 level. Revenues have also doubled but net income has declined. Employment growth has not kept pace with the increase in passengers or the increase in revenue, growing by only 8 percent.

The question raised by this subcommittee, is how does deregulation impact the rural economy? Concerns about the safety of the new airlines, the congestion of the airways, the ability of the comptrollers to handle the increase in traffic, airline delays, overbooking and continual mergers have been well chronicled. They are tertiary concerns to the rural economy.

Rural areas worry about the downward economic spiral that results from poor quality airline service. They worry about maintaining a link to the large, urban areas. They worry about attracting new industry and tourism Businesses do not want to locate in areas that are not accessible to travel by industry personnel or for shipping and receiving of industry equipment, parts or finished goods.

This also affects tourism in various areas. Getting to a vacation spot should not be an arduous journey for the tourist. They should not have to worry about connecting flights with long stopovers and the safety of the small regional airlines. Rural areas worry that these travelers may opt for a different destination if the process is difficult and the cost is exorbitant. Many rural areas cannot afford to lose new business opportunities, small business growth and the tourist market because of poor airline service.

Currently, Essential Air Service (EAS) is a vital element in rural air travel but it is not the answer. It is simply a floor from which to build.

I thank you, Mr. Chairman, for holding hearings on this issue. Maintaining the health of the rural economy is of great importance to this country and having a viable air transportation system is an essential element contributing to that health. I thank the witnesses for taking the time to come and testify before this subcommittee and look forward to hearing their views and suggestions on this most important issue.

STATEMENT BY SENATOR ALFONSE M. D'AMATO
BEFORE THE SUBCOMMITTEE ON THE RURAL ECONOMY
AND FAMILY FARMING
OCTOBER 28, 1987

MR. CHAIRMAN, I WOULD LIKE TO WELCOME TO THIS SMALL BUSINESS SUBCOMMITTEE THIS MORNING OUR DISTINGUISHED PANEL OF WITNESSES WHO REPRESENT BROAD INTERESTS IN THE FIELD OF AIRLINE DEREGULATION AND ITS IMPACT UPON THE RURAL ECONOMY.

AIRLINE DEREGULATION HAS BROUGHT ON MANY CHANGES WITHIN THE INDUSTRY. SOME OF THESE CHANGES HAVE BEEN FAVORABLE WHILE OTHERS HAVE BEEN CAUSE FOR CONCERN. SOME OF THE MOST MENTIONABLE BENEFITS THAT HAVE RESULTED FROM DEREGULATION ARE: THE DRAMATIC DROP IN THE PRICE OF AIRFARE; THE INCREASE IN THE AFFORDABILITY OF FLYING; AND AN INCREASE IN THE NUMBER OF AIRLINES: FROM 36 TO 74. THE NUMBER OF WORKERS EMPLOYED IN THE AIRLINE INDUSTRY HAS ALSO RISEN BY 29,ØØØ IN 1978 TO 362,ØØØ IN 1986.

THE DOWNSIDE TO DEREGULATION HAS BEEN A SUBSEQUENT INCREASE IN AIR TRAFFIC AND THE UNREALISTIC NUMBER OF FLIGHTS SCHEDULED TO TAKE OFF AND LAND AT THE SAME TIME. THERE HAVE ALSO BEEN NEGATIVE EFFECTS UPON AIR SERVICE TO THE MORE RURAL AREAS OF THE COUNTRY. THE MOST OBVIOUS PROBLEMS CENTER

AROUND HIGHER FARES AND AN INCREASE IN CUSTOMER DISATISFACTION WITH THE QUALITY AND QUANTITY OF SERVICE TO SMALL COMMUNITIES. BETWEEN 1978 AND 1984, THE NUMBER OF COMMUNITIES REACHED BY SCHEDULED AIR SERVICE FELL TO 541 FROM 632, LEAVING 91 CITIES WITHOUT AIR SERVICE.

IT APPEARS THAT THE ONLY SALVATION FOR THE RURAL COMMUNITIES THAT HAVE BEEN ADVERSELY AFFECTED BY DEREGULATION IS THE ESSENTIAL AIR SERVICE PROGRAM ESTABLISHED IN 1978. THE COMMUNITIES THAT HAVE BEEN SERVED BY EAS ARE CONCERNED OVER THE FACT THAT ITS SUBSIDIES ARE SCHEDULED TO SUBSIDE ON OCTOBER 24, 1988. WHILE THERE ARE PROBLEMS WITH EAS, IT STILL REMAINS AS THE ONLY ALTERNATIVE AVAILABLE TO SOME SMALL COMMUNITIES.

I LOOK FORWARD TO THE TESTIMONY OF OUR WITNESSES THIS MORNING AND TO THE INSIGHT THAT THEY ARE SURE TO PROVIDE THIS COMMITTEE ON THE IMPACT OF AIRLINE DEREGULATION UPON THE RURAL ECONOMY.

THANK YOU, MR. CHAIRMAN.

STATEMENT OF ROBERT W. KASTEN, JR.

HEARING BEFORE THE SMALL BUSINESS COMMITTEE'S SUBCOMMITTEE ON RURAL ECONOMY AND FAMILY FARMING

"The Effect of Airline Deregulation on the Rural Economy"

October 28, 1987

Thank you, Mr. Chairman. I commend you for your leadership in looking into the effects of airline deregulation on the smaller communities. We have all heard the numbers and statistics that do indicate the general positive effects of deregulation as far as decreased fares and increased numbers of citizens flying are concerned. But the fact that one can fly from Washington to the west coast cheaper than from Washington to Superior, Wisconsin, is not always recognized.

Further, we have all experienced the frustrations of the flying public in the service end of things, on both the long and short flights.

Because of the tie-in between economic development and air service availability, the small communities that have been hit the hardest with the economic plight of the farms, are disadvantaged in their attempts to diversify their economies if

they cannot guarantee air service to prospective employers. And yet I don't think that every community deserves air service if the load factors are not there.

Serving on the Aviation Committee of the Commerce Committee we have held hearings on the continued authorization of the Essential Air Service program, and I am pleased that that committee and this hearing are exploring the problems of the rural areas before we have our backs to the wall as far as legislative time is concerned. By the expiration of the current authorization next year, I hope that inquiries and hearings will help to develop a workable and equitable solution to the particular problems of rural America's air service.

I look forward to hearing today's testimony, ~~and~~ reviewing this record and working with you, Mr. Chairman, and with the other members of the Commerce Aviation Subcommittee in protecting the advantages of deregulation and fine tuning its application in the low density markets.

The CHAIRMAN. Gentlemen, I wonder if you could provide us with a few more anecdotes. I think that Mr. Anderson was correct when he stated that we do not have any solid, comprehensive data on the effects of airline deregulation on economies in rural America, but we all know of many instances where reduced service has dramatically hurt the community.

I am wondering if you could also give us some examples or anecdotes of how the senior citizens will tend not to travel by commuter airlines because of the inconvenience and noise the small and cramped surroundings or the feeling these planes are unsafe.

Another area is tourism. I know that many folks from more densely populated parts of our country and even folks from other countries would like to visit rural America. I am wondering if you could give us some anecdotes or examples that you know of where tourism to rural America is reduced, impeded or threatened because of airline deregulation?

We'll begin with Mr. Schofield.

Mr. SCHOFIELD. Thank you, Senator. With regard to tourism, a number of our communities have developed—as one part of tourism—convention centers to be able to hold some of the regional and national conventions. It has been very difficult for them to secure these conventions with existing air service.

We are in the process of doing an air service study, which hopefully will be able to provide us with actual numbers of what is happening in these particular cases. I do know that in the case of Pierre, which is the capital and is also prepared for hosting conventions and have recently built a new convention facility, that one of their problems is adequate air service to get the regional people into the community to attend the conventions. So as a consequence, they do not get a lot of regional conventions but they are capable of handling them.

With regard to our senior citizens and our handicaped people, we have a very difficult time with our commuter airline service. They are just not really capable of handling their people. The people just do not feel comfortable in getting aboard these airlines.

We are finding a number of cases that where, if they can afford it, they will drive to the larger cities where they can board bigger airplanes and that way make their final destination. But it is very important that they have the opportunity to be able to, from their own home city, board an airline and be able to go to their destination. I feel that they are not taking advantage of that opportunity because of the smaller planes and facilities provided by the commuters.

The CHAIRMAN. Mr. Pankey, do you have any examples?

Mr. PANKEY. Yes, I would like to share with you that I was the director of aviation at Springfield, IL, prior to going to Missoula, MT. As you know, Springfield is the State capital of the State of Illinois and the home of Abraham Lincoln and Lincoln's Tomb that attracts 2 million plus visitors annually to the community, both nationally and internationally.

That community today has no major scheduled airline service. American and Ozark discontinued service. The State capital of 100,000 plus has to deal with the small aircraft problems. The communities were asked to invest millions of dollars in building run-

ways that would accommodate jet aircraft, the DC–9 for example, back in the 1960's.

A lot of communities went out and spent millions of dollars extending their runways for those aircraft, building their terminal buildings, their jetways, all the security requirements for that size of aircraft. Then they woke up one morning and found that not only were they abandoned by the large jet equipment, but they had empty terminal buildings and long runways that they no longer needed for the small aircraft that was serving them.

So I think that sort of a disservice, if you will, took place and a lot of unnecessary dollars were spent. We are going backward instead of forward.

The CHAIRMAN. Mr. Anderson, do you have any examples?

Mr. ANDERSON. With regard to the seniors, Mr. Chairman, most of them cannot afford it. I know from International Falls to Minneapolis, the round-trip ticket rate now is $428.

The CHAIRMAN. That is a very good point. I have heard about that, too. I think that the fares are so high in the smaller communities they stay in the hubs because they cannot do it, the fares are so high.

Mr. ANDERSON. We are a distance from International Falls to Minneapolis/St. Paul. It would be similar from Washington, DC, to Cleveland, OH. I know that you can fly to Cleveland much cheaper than you can from International Falls to Minneapolis.

The other part of that is that we do not have any other rural transportation. I should not say that we do not have any, because we have one bus that comes in at night and goes back out in the morning. That is the extent of other transportation. Other than that, we give them a ride around town, but that is about it.

In the area of tourism, our chamber of commerce spends tens of thousands of dollars each year to go out to sport shows, trying to bring fishermen and hunters in. And as I told you, the airplanes cannot accommodate their tackle boxes, they cannot bring in a hunting dog with them. They cannot come into South Dakota or Montana to go hunting either, because those planes just cannot carry dogs with them. You cannot pack dry ice and bring your game out with you.

These are just some of the problems that they posed to the chamber of commerce when you go to a sports show. They tell you, there is no use flying to your area because I just cannot enjoy myself and end up with a lot of hassles.

The last example that I would use is one that in my private employment with Boise Cascade Corp. they have a paper mill in International Falls, and we need to keep paper machines running all the time in order to make a profit. Downtime is critical to us, and if you cannot get equipment in that may be 200 pounds, you are just not going to run those paper machines.

So, we have to have trucks constantly running back and forth 300 miles to the Twin Cities in order to keep those paper machines running for our equipment.

The CHAIRMAN. I have heard of an example that I think is astounding, frankly. I have heard that a large, important country in the World that has been working with some U.S. businesses promoting American tourism will not schedule flights to parts of

America where the end destination points is commuter service. They will not do it, will not do it.

That is, they will only schedule flights where the end destination point is by jet service, I think basically for the reasons that a lot of you are indicating. That is, noise, delayed or cancelled flights and inconvenient schedules, to name a few of the reasons. I also suspect they are concerned about safety, not to mention the exorbitant fares they have to pay to fly to less-populated areas.

It seems to me that one problem we have here is a lack of incentives to encourage the airlines to provide more service to our less-populated areas. Because the major airlines have alliances with most commuter airlines serving a particular area, competition is lacking. Without competition, there is no incentive to provide better service.

Do any of you have ideas as to how we can build in some incentives so that carriers will not only begin to provide more service but also provide different equipment, the kind of equipment that can service the peoples needs in rural America?

Mr. ANDERSON. Certainly, I would take a crack at that, Senator. It seems to me that one of the things is to have airline agreements between the major carriers and the air links or whoever they might be that are serving the smaller communities, in hopes that they will be able to work together and get some lower fares.

A majority of the passengers are going beyond the hub. Although there is certainly a lot traffic to the hubs, we do need to have that kind of agreement, I think. I think that there needs to be some type of an incentive there for them to have it, and I do not think the EAS bill touches on that. To some degree it encourages it, but it does not really force it. I think that is part of the problem in a lot of areas, as you have well spoken of.

It seems to me that we also need to be having the communities work with the air carriers. We have gone out and done advertising for our airline or our air carrier to try to get the people to use the airports more. Certainly, it may need to be two, three or four things that we need to do to try to encourage people to use that airline in hopes that they are going to go out and get bigger equipment to take care of it.

We have held hearings in the community and asked the airlines to be there, told them what our needs are, but this does not seem to sink in at this point.

The CHAIRMAN. Do you have any ideas, Mr. Pankey?

Mr. PANKEY. The controlling influence is, I think, that the airports have very little input in. For an example, airline costs, the only thing that we have any control over is the landing fee and an office rent, and that is only 5 percent of their total operating costs with their salaries, equipment, and fuel and everything else being the majority.

You might say that well, maybe we can give them a break and lower the landing fee or something else. It is just a small item when they are using that airplane with the 70 percent load factor at our city to make money, they will run it between the high volume points where they can get an 85 percent load factor and make more money.

The CHAIRMAN. Mr. Schofield.

Mr. SCHOFIELD. I would just like to say that one of the things as we have done is to meet with the commuter airlines. They have always asked us for a great deal of technical data or backup data for our plane. We talk about marketing, and one of the things that we are trying to do is provide them with data to show them where there are instances that they could; by lower fares, increase their ridership, and so forth.

The CHAIRMAN. What if you just briefly address the fairness, or in my view the unfairness and the inappropriateness of assuming that because rural communities do not generate quite as many passengers or have quite as many folks or certainly not as much revenue as the major cities in this country, that therefore they should be just forgotten?

What about our interstate highway system, our primary highway system in America, Americans have always thought it was important to provide a good highway system throughout this country, including rural America, to enable citizens to travel to every part of the United States. If we would have applied some logic to building our highway system as is now being applied to air service, rural communities would not have any primary highways. They would not have them, period. You would be able to drive between the major cities. But you would have to get on your horse and buggy and traverse a dirt road to go out to rural America.

Another point: There are many Federal programs for urban America that are paid for by citizens across the country—including those living in rural America. For example, the Metro System here in Washington, DC, cost $6 billion. Only 20 percent of that amount is paid for by fares. A full 80 percent of the Metro System is paid for by taxpayers across this country.

We as Americans, are paying for the Metro System in Washington because we want a good metro system in our Nation's Capital. Just as the Nation believes it is important to provide an interstate highway system and a postal service to urban as well as rural America, I believe it is important to provide an adequate transportation system. It should be a national system.

We all know that there is less service transportation to parts of rural America. I wonder if the three of you could comment very briefly on the philosophy of a national system and the importance of the national system as it applies to airline service?

Mr. ANDERSON. Mr. Chairman, I certainly think that a small transportation system including air, rail and highways certainly is going to help ensure a strong national economy because without a doubt, most of our natural resources are out in rural America. Not speaking of people being a natural resource at this point; they are not.

We certainly need to have a strong transportation system to ensure that this country is going to have a strong economy that is going to be able to play a part in making this a continued leader in the World.

Mr. PANKEY. Something has obviously gone wrong in our air transportation industry in the last year or so with the mounting number of complaints that you are receiving and we are receiving as airport operators from the customers.

Maybe a blueribbon or some type of committee needs to be appointed to really investigate this whole industry, not only the FAA problems but the airline problems as well. I am sure that we could all give that a little thought and give you some input into that, and I would be happy to do that.

The CHAIRMAN. Great minds think alike. Mr. Schofield.

Mr. SCHOFIELD. I would echo what the other two members have said. Rural America must be tied to the rest of America, and transportation is very important to the economy. Rural America is the breadbasket of America, for instance, the rural areas provide the food the rest of America uses as well as part of the world. It is important that rural America be tied with transportation facilities to the rest of the World.

The CHAIRMAN. I have taken too much time. Senator Karnes, do you have points or questions?

Senator KARNES. Thank you, Mr. Chairman.

STATEMENT OF HON. DAVID K. KARNES, A U.S. SENATOR FROM THE STATE OF NEBRASKA

Senator KARNES. First of all, I compliment my colleague from Montana for calling these hearings, because of the fact that this is a very important issue for my State of Nebraska.

Some of you may not know this, but the Chairman is one of the outstanding runners in the Senate. Now I understand with all the transportation problems that I am hearing about, why he has developed that skill. [Laughter.]

I know that Montana is a very big State, and better transportation of all sorts would be a great boom not only to Montana, but to my State of Nebraska.

Mr. Chairman, I would just like to read a couple of items from a *Wall Street Journal* article, October 5, 1987, entitled "Country Blues." It talks a little bit about my State of Nebraska and some of the air problems that we have encountered in the State. I think that they are very illustrative of the frustration that we are seeing and the difficulties that we are experiencing as we attempt to deal with some problems in the agricultural economy. Also, an effort that my State has made to diversify the rural economic base and how continually when we make an effort on one hand, sometimes it seems like we are taking one step forward and two steps back when we bring in people and it takes them 3 days to get to where we are telling them that it is a great place to be.

I just might quote from this article, and then I would like to have the remaining portion of the article submitted for the record. I quote: "As Scotts Bluff's mayor Donald Overman recalls that unpleasant morning several years back, snow was blowing out of a leaden sky when his eastbound Frontier Commuter Airlines flight set down at North Platte, NE.

As soon as the door popped open, the crew hastily departed, leaving the plane sitting alone on the tarmac with Mr. Overman and 20 other bewildered passengers waiting to fly on across the State. The pilot returned to announce that the airline was jettisoning its unprofitable route across Nebraska.

He, at that time, gave the passengers a choice: Fly 200 miles in the opposite direction to Frontier's home base in Denver or stay dumped in North Platte. Mr. Overman calls it a pretty dramatic lesson in deregulation. [Laughter.]

At his insurance agency in Scotts Bluff, Mayor Overman keeps a plastic model of a passenger jet behind his desk as a reminder since Scotts Bluff has, indeed, managed to hold on to some air service since deregulation, but they have done this at a price. There are no super savers or fare wars experienced in Scotts Bluff.

Since 1984, four airlines have come and gone, including the one that stranded Mr. Overman in North Platte. The 150 mile flight to Denver now costs $75, up from $49 3 years ago. A 1982 Federal study showed the following about deregulation:

The average cost of flying out of a small town in rural America had climbed by 16 percent, while the cost of flying out of big cities had declined by 33 percent. A Federal Aviation expert admits that those percentages are still, today, pretty much in the ballpark.

Again, that just underscores the frustration that many of us have in the rural communities, and I am preaching to the choir I know, when I talk with the members that are here to testify.

There have been some good and positive results from deregulation. I would be the first one to admit that Nebraska has benefited from some of the positive things of deregulation. But we need to be very careful that we do not cut off our nose to spite our face.

As we look at the beginning of pheasant season, a lot of people come to Nebraska and would like to bring their dogs and their game out of Nebraska. They will have to probably do that by truck and we are running into deregulation problems with that too.

I might again compliment my colleague from Montana and compliment the people that are here today. I do believe that we should be studying this issue much more carefully and bring some of the collective intelligence that is assembled in this room today to focus specifically on the air transportation industry and how it impacts the efforts that all of ours are making in rural America to diversify our economic pace and assist those people who have been a part of production agriculture to transition into other economic opportunities.

I think providing essential air service and reasonably scheduled air service to these communities will help Nebraska a great deal and will be very well received.

I just want to compliment Mr. Schofield on his observation which is, rural America must continue to be connected with the rest of America. I think that sums it up very well. We want to make sure that rural America continues to be a very important economic part of our country, and I believe very strongly that it will if we can continue to be ever mindful of the needs of transportation to rural America.

Mr. Chairman, that is all that I have. I again, compliment you for calling these hearings and having this fine group of people testifying for us today.

[The article referred to follows:]

Country Blues

Deregulation Raises Prices, Cuts Services In Many Rural Areas

Phone Bill of Mrs. McGinnis Is Up 300% in Nebraska; A Sick Man Misses the Bus

Small-Town Banks Play Safe

By Bill Richards
Staff Reporter of The Wall Street Journal

SCOTTSBLUFF, Neb.—As Scottsbluff's mayor, Donald Overman, recalls that unpleasant morning several years back, snow was blowing out of a leaden sky when his eastbound Frontier Commuter Airlines flight set down at North Platte, Neb.

As soon as the door popped open, the crew hastily departed, leaving the plane sitting on the tarmac with Mr. Overman and 20 other bewildered passengers waiting to fly on across the state. The pilot returned to announce that the airline was jettisoning its unprofitable route across Nebraska. He gave the passengers a choice: Fly 200 miles in the opposite direction to Frontier's home base in Denver or stay dumped in North Platte.

Mr. Overman calls it "a pretty dramatic lesson in deregulation."

For big-city dwellers, deregulation has mostly been a boon. Wider freedom from federal rules has often led to cutthroat competition in everything from interest rates to intercity flights and telephone calls.

Different in the Panhandle

But in sparsely populated places like the Nebraska Panhandle, deregulation hurts. Although some 700 banks have branches in New York City and about 40 airlines fly in and out of Chicago, a rural area frequently has only a single supplier of such vital services.

So as regulatory control fades, prices are climbing in these areas—and service is dwindling. From banks to buses to telephones, deregulation is driving home a hard economic lesson: Big government may not fit with the rural self-image of rugged individualism, but no government is sometimes worse.

"Rural people place great value on the idea of self-sufficiency, but they operate in a framework that is anything but independent," says George W. Rucker, research director for Rural America, a Washington D.C. public interest group. Mr. Rucker and others say that federal regulation has long amounted to a subsidy of low-price rural power, transportation, telephone and other services, acting as a form of social engineering to build and maintain rural populations. "In a sense," says Calvin Beale, a U.S. Agriculture Department population expert, "rural development was propped

WALL STREET JOURNAL

October 5, 1987

Speeding Depopulation?

Deregulation is underscoring the extent of those hidden rural subsidies as it wipes them out. Mr. Beale and others worry that the process is also hastening the depopulation of some of the same communities that regulation once helped build.

"If the present deregulation trend continues," warns Sen. Larry Pressler, Republican of South Dakota, a longtime opponent of the trend, "small cities and towns could end up as remnants of the past."

Since the beginning of the 1960s, nearly half the nation's nonmetropolitan counties have lost population, reversing the widely publicized back-to-the-land trend of the previous decade. Agriculture's problems, farm consolidations and the aging of the rural population have all contributed. "But when you deregulate," says William S. Duncan, head of the Mountain Association for Community Economic Development in Berea, Ky., "you're making a social decision to become a nation of big cities."

On the high plains of western Nebraska's Panhandle, a region that is as large as all of lower New England but has a population of less than 100,000, deregulation's impact isn't like that of the dust storms and droughts that sent farmers stampeding in years past. Instead, it is more like erosion, making life a bit more expensive here and a bit less palatable there.

The Telephone

At her desk in Crawford, Neb.'s tiny city hall, Mary McGinnis, 65, holds forth about her telephone bill from Northwestern Bell Telephone Co. "Can you believe?" Crawford's white-haired water commissioner tells a handful of loungers. "The bill on that old el-cheapo dial telephone of mine, it went up nearly 300% since 1984"—from $7 a month to $27.

In the past, the Federal Communications Commission required telephone companies to charge urban and rural customers the same for service, in effect subsidizing rural service, which is far more expensive because there are far fewer customers to cover fixed costs. But since deregulation, phone companies are passing on more of the actual service cost to their customers, and rural phone bills are soaring.

By itself, a rising phone bill isn't likely to send anyone packing for the city. Still, Mrs. McGinnis says she sometimes finds herself thinking the unthinkable these days—contemplating a move to a bigger place, like Rapid City, S.D. "It would be nice," she says, "living close to where things are cheaper."

The Bus

William Shay is one of a contingent of disabled veterans around Scottsbluff who travel regularly to Veterans Administration hospitals for treatment. He suffers from edema. Twice a month, the 70-year-

old former farm laborer leaves his rented room so that doctors can drain off the fluid t balloons his weight to 290 pounds.

Mr. Shay, who has had two heart at-cks, used to take the bus to the veterans' h spital in Hot Springs, S.D., some 150 miles north of Scottsbluff. Then came de-regulation and the bus route was eventually dropped. Now he waits for the local veterans' office to find him rides and doesn't always get to the hospital on schedu e. "That bus," he says, "was the difference between life and death for me." Now his life depends on a more haphazard arrangement.

Since bus deregulation began in 1982, more than 3,000 small towns and cities have lost bus service, according to the Department of Transportation. Star Bus Lines, the Panhandle's last remaining local carrier, still has travel posters for Hawaii and Australia on the walls of its Scottsbluff terminal. But a bus traveler headed for one of those exotic destinations must first take Star's 6:30 a.m. bus 40 miles south to Kimball, Neb., then catch the westbound Greyhound for Cheyenne, then wait for the bus south to Denver. The 250-mile trip takes a day and a night. Few people bother.

Darlene Ruth, Star's manager, says the bus line is thinking about ending its scheduled runs and just offering charter service. Under deregulation, big carriers like Greyhound Lines Inc. juggle schedules and routes so fast, Mrs. Ruth says, that feeder operations like Star can't keep up. "You get the impression they don't care about us little people in between the big cities," she says.

Trucks

Richard Holliday, a blunt-spoken former trucker whose Gehring, Neb.-based Nebraska Transport Co. is the region's biggest truck line, says that since deregulation he has routinely slashed rates for customers on highly competitive interstate-highway routes. But customers in communities off the beaten path, where there is little truck competition, have to pay more than their urban counterparts. Mr. Holliday offers a gloomy prediction for some of the industry's customers: "The mom-and-pop store in some small, out-of-the-way town—they've had it."

In a corner booth at the 77 Lounge in Chadron, Neb., far from any interstate, owner Evva Gore whips out a freight bill to show a visitor just how fast her trucking costs are climbing. It costs $13.55 to have three cases of liquor hauled 400 miles across the state from Omaha, up from $12.78 last year.

"When I saw that I said 'bull-ers,'" says Mrs. Gore, a 27-year vet-of the bar business. The 77 Lounge is up for sale—not because of deregulation—and Mrs. Gore says she is looking forward to moving someplace warmer. Meanwhile, she confides that she has worked out a way to beat the price increase: "I drive my motor home to Omaha and tell them to fill

Not everyone in Chadron's business community can improvise like Mrs. Gore. James Aspden, manager of Henkens Implement Co., wends his way between bins stuffed with spare farm-machinery parts and stops in front of a 16-foot sickle bar. Mr. Aspden says the device costs only $150, but he has to tack on $50 more to cover trucking charges. When a freak hailstorm caused $25 million of damage to the town last summer, Chadron residets discovered they could find replacements for their shattered storm windows for $20 less in towns with better truck service.

The Bank

When Robert McCulley turned up at the Holiday Restaurant in Kimball, Neb., one evening this past July, more than 50 people crowded into the back room to meet him. Mr. McCulley is no celebrity; he is a broker for E.F. Hutton & Co. And like a growing number of bankers, brokers and other money managers these days, he spends much time in small towns and cities around the Panhandle trying to persuade people to put their money elsewhere than the local bank.

Deregulation means more business for Mr. McCulley and his fellow circuit riders. But it is sapping life from small-town banks and from the communities that rely on them. Under deregulation, many rural banks are forced to pay higher interest to compete with outsiders for deposits. Deregulation has also cleared the way for big outside banks to steal away borrowers who once automatically would have gone to their local bank for cash.

In a report on changes in rural America last year, researchers at the Kansas City Federal Reserve Bank weighed the pros and cons of bank deregulation and concluded, "On balance, economic activity in many rural communities probably has been negatively affected by higher [loan] interest rates from deregulation."

Michael Nelson, president of Kimball's First State Bank, estimates that 25% of the money the town's 3,500 residents might have deposited in his bank in the past now goes to brokerage houses and other outsiders. Squeezed for profits, small-town banks are shying away from putting money into uncertain local business ventures. "These days," says Lewis Mehling, vice chairman of American National Bank in Sidney, Neb., "you're a little less inclined to stick your neck out to help some young person get started."

Mr. Mehling's bank recently turned down applicants seeking business loans to launch a restaurant and a retail store in Sidney. There isn't much likelihood the businesses will get help elsewhere. "E.F. Hutton," Kimball's Mr. Nelson points out dryly, "doesn't finance gas stations and clothing stores."

The Plane

At his insurance agency in Scottsbluff, Mayor Overman keeps a plastic model of a passenger jet behind his desk. It is a talisman of sorts, since Scottsbluff has managed to hold on to some air service since deregulation. But at a price. There are no Supersavers or fare wars. Since 1984, four airlines have come and gone, including the one that stranded Mr. Overman in North Platte. The 150-mile flight to Denver now costs $75, up from $49 three years ago.

(A 1982 federal study showed that following deregulation, the average cost of flying out of a small town had climbed by 16% while the cost of flying out of big cities had declined by 33%. A federal aviation expert says those percentages are "still in the ballpark today.")

Mr. Overman isn't complaining about the price. He has been to Washington twice recently pleading for federal help to keep Scottsbluff's air connection alive. The city is 400 miles from Lincoln and Omaha, Nebraska's state capital and its financial center. Without air service, the mayor says, "we might as well be in another country."

Other Panhandle communities are even more worried. Since deregulation, virtually all the region's air service depends on the federal government's Essential Air Service program, which provides subsidies to commuter lines servicing otherwise unprofitable rural areas. The program is scheduled to end next year.

Panhandle officials say that losing air service would be deregulation's cruelest blow. Without it, a distant traveler who wanted to get to Chadron would have to fly to Rapid City, the nearest city with scheduled air service, hire a car and drive 114 miles to reach Chadron. "It would have a drastic effect on our economic development effort," says Carl Dierks, Chadron's city manager.

Among other problems, Mr. Dierks points out, there would be no air link for nearly 2,000 students who attend Chadron State College, the community's economic anchor. Mr. Dierks is heading an effort to broaden Chadron's agriculture-based economy. But he says one of the first things prospective employers ask about is air service.

"Disaster might be too strong a word to describe the effect of losing our air service," Mr. Dierks says. "But it would certainly make Chadron a less desirable place to live."

The CHAIRMAN. Thank you very much, Senator.

One final, quick question because I only have about 2 minutes left before we have to adjourn for a vote.

You mentioned, Mr. Pankey, that perhaps there is some cross-subsidization here. You suggest that some of the urban routes in some respects are partly subsidized by some rural routes.

I wonder if any of the three of you would provide me with your thoughts on whether there is any of that going?

Mr. ANDERSON. Speculative, Mr. Chairman.

Mr. SCHOFIELD. The same way, just speculative.

The CHAIRMAN. On that point, we will recess the hearing for about 10 minutes.

Mr. PANKEY. I wonder if written remarks will be part of the record?

The CHAIRMAN. Absolutely. The record will be kept open for 10 days as well. In addition to that, your prepared statements will automatically be made part of the record.

We will recess for 10 minutes.

[A brief recess was taken.]

The CHAIRMAN. The Subcommittee will resume the hearing. Our witnesses on our next panel include Mr. Morten Beyer, who is the president of Avmark, Inc.; Mr. John Nance, who is a writer/author in Tacoma, WA; and, Mr. Stephen Dempsey, professor of law and director of the Transportation Law Program, University of Denver College of Law in Denver, CO.

Gentlemen, we are happy to have you here. Mr. Beyer, why do you not lead off?

STATEMENT OF MORTEN S. BEYER, PRESIDENT, AVMARK, INC., LOLO, MT

Mr. BEYER. Mr. Chairman, my name is Morten Beyer. I am a President of Lolo, MT, and President of AVMARK, Inc., aviation consulting firm, with offices in Montana, Arlington, VA, and London, England.

I have been in the aviation business for more than 40 years. In my remarks here today, I want to focus briefly on the major structural changes which have occurred in the airline industry under deregulation. I will show briefly, the impact that it has had on air service to small communities nationwide and then concentrate on some of the direct effects it has had on Montana.

As shown on chart 1 here, there has been a dramatic mortality rate in the industry since 1978, resulting in an increasing consolidation of airlines large and small.

The 11 major airlines have shrunk to eight; the eight former local service carriers are now two and they are trying to merge; the eight original low-cost charter airlines have been reduced to one, through bankruptcy and abandonment; 14 former regional airlines have shrunk to only four; over 100 new upstart airlines were certificated by the CAB and about 32 got off the ground and most of those crashed, leaving only a handful still operating; of the 50 top commuters in existence in 1978, 29 have disappeared and others have risen to replace them.

Today, the top 50 commuter carriers who constitute 90 percent of that industry are captives of the major carriers, in part or in total owned, controlled, and financed by the giant airlines and relegated to serving the big airlines at their hubs.

Chart 2 presents typical examples of this feeder commuter service and shows here that they look like little starbursts into the major hubs. The linear service, which characterized our air service in the prior period has largely disappeared.

There has been a shift away from the smaller communities to the larger traffic-generating points by the certificated route air carriers. Thus, by 1985, aircraft departures at the large and medium hubs increased by 29 percent over 1978. During this same period, aircraft departures at the small non-hubs decreased by 31 percent.

The impact of this service shift is seen in the respective traffic generation. At the large points passenger enplanements increased 55 percent, while the smaller points have shown a decline. This shift away from smaller communities and the increasing captivity of commuters have had a catastrophic effect on air service in the United States.

Chart 3, the map there in colors, the black points there show the 140 communities in this country that have lost all service under deregulation. There are additionally, 190 points—shown by red dots—which represent cities which used to receive service by the major and local service carriers, jets and large turbo props that today have been relegated solely to commuter services.

As we said earlier, the vast bulk of this service is solely to the nearest hub of their major masters. There is no question that the major hubs are receiving more service, many would argue too much as more and more flights are jammed into the hubs and fewer provide linear service to and between the smaller cities and communities.

And there has been, of course, a plan to drop the essential air service program entirely. Today, according to publications of the RAA which is the Regional Airlines Association, there will be 316 communities which would additionally lose all, or have a reduction of, air service if the central air service were dropped and they were unable to replace it.

Prior to deregulation, 14 cities in Montana received scheduled air service by four airlines. Montana has been relatively lucky—no city has lost all air service. But the quality has been seriously eroded in terms of aircraft type, size and route patterns. Let us look at the picture.

That chart shows in black, the current jet air service in Montana. The red lines represent services which have been deleted in their entirety with jet aircraft. Those include from Great Falls to up north to Canada to Kalispell to Spokane to Seattle. Services from Missoula to the west, Helena to the west, Butte to the west and Bozeman to the west, all have been deleted.

Billings has lost three of the destinations that it used to have: Chicago, Fargo, Bismarck.

Senator PRESSLER. I would just like to ask a question, the black lines are what?

Mr. BEYER. The black lines are the existing jet service.

Senator PRESSLER. They go into Minneapolis/St. Paul. They are from where, what cities?

Mr. BEYER. Minneapolis/St. Paul has direct service from Great Falls and Billings only. These are airline codes.

Senator PRESSLER. Denver is more your regional hub?

Mr. BEYER. Denver, Salt Lake. Salt Lake actually gets the bulk of existing services, but even it has lost some of the direct service it once had.

[The prepared statement of Senator Pressler follows:]

STATEMENT OF SENATOR LARRY PRESSLER
BEFORE THE
SUBCOMMITTEE ON RURAL ECONOMY AND FAMILY FARMING
OCTOBER 28, 1987

Mr. Chairman, let me first thank you for scheduling this hearing on the effects of airline deregulation on the rural economy. Over the past nine years, airline deregulation has had a devastating impact on our nation's smaller communities and rural areas. It is time to make necessary adjustments to ease the negative results of deregulation and improve our overall air transportation system.

In the Commerce Committee, on which I serve, we have held hearings on the Essential Air Service program. EAS provides the only assurance that air transportation will continue to be available to less populated areas, guaranteeing the smaller communities a certain level of service. If we do not act quickly to extend the EAS program before it expires next year, air service no longer will be provided to many of our nation's smaller communities and rural areas.

In addition, we have just begun hearings on safety and re-regulation of the airline industry. I will save most of my comments on this subject for those hearings, but wish to state that improvements in the air service industry can and must be made.

I opposed the 1978 airline deregulation legislation when I was in the House of Representatives because I anticipated many of the problems now taking place. Flight delays and misplaced baggage are a few of the inconveniences experienced by consumers across the nation. However, our smaller communities are also faced with the very serious problem of receiving only limited air service or no service at all.

Air transportation is an important link between the smaller communities' and the outside world. It is a vital element in every state's economic development program and is necessary for industrial expansion. An example from my home state might be helpful. The City of Yankton, South Dakota, is working to bring new businesses into its community. One of the biggest problems faced by that community is the uncertain future of air service. Efficient air transportation is an essential criterion for any business or other major enterprise seeking to locate in a particular area. Yankton is an EAS community. Before it can attract a prospect to locate there, it must be able to ensure a stable airline service. My point is that, for the hundreds of Yanktons around the country, air service is a key component of any local economic development program.

I am pleased to welcome Dean Schofield from South Dakota's Department of Transportation. Dean will have the opportunity to testify later today and further address the importance of adequate air service to smaller communities and its impact on economic development.

Mr. BEYER. There has been a deterioration in the number of places or the whole areas that you could get to from Montana on a jet airplane. Let us look at the commuter picture.

The black lines here represent the commuter system in effect in 1973. At that time, Frontier was provided a linear service across the High Line from Glasgow and Williston, Wolf Point, Havre, and Great Falls and the service to Great Falls to Lewiston, from Billings down to Sydney, Glendive, and Miles City and to Billings.

Those services have all been deleted. Today you have only services that go out and back from Billings to Wolf Point and Glasgow, and another one to Williston and Sydney, and the third one to Glendive and Miles City.

The quality of aircraft has been reduced. In the 1970's Frontier operated Convair 580's on the High Line. They have been reduced to twin service and Big Sky came in when Frontier pulled out entirely where they were trying to service the State. They put on Metros and Jet Streams and pressurized airplanes, but under the pressure of EAS they had to reduce those to non-pressurized Cessnas; two engines, eight passengers and the pilot.

There has been a growth of commuter service to the west, as Horizon and Big Sky have tried to fill the gaps created by Northwest and other airlines pulling out. For its regional transportation, today Montana is largely dependent on commuter airline services.

Now, what happened to traffic in this period? When the jet service was improved in the 1970's in Montana, traffic increased anywhere from 78 percent total passengers who boarded at Great Falls to 363 percent at a point like Bozeman. The increase in the small cities was very much less.

The clear indication is that the traffic responds to the presence of service. Of course, since the substitution of smaller airplanes, the traffic has fallen off. Montana as a whole in 1987, has seen traffic fall from 223,000 passengers in 1978 to 201,000 passengers today. That is in a country where overall traffic is supposed to be up 40 percent or so.

A horrible thing has also happened——

The CHAIRMAN. Mr. Beyer, if you will summarize and give a little overall. If you can summarize, please.

Mr. BEYER. Another horrible thing has happened to fares in Montana, that this chart will show. Fares have increased by 300 to 400 percent. It used to cost $46 to go from Wolf Point to Billings. Now, it costs $212. You can fly across the Atlantic Ocean for that.

I have been asked to suggest what should happen to EAS. One, it is currently designed to provide the minimum service with the smallest airplanes, on the fewest days of the week to as few cities as possible.

You could strengthen the EAS by simply enforcing the intent of the original act to provide decent service to the communities and mandate that more money be given and that higher service standards be expected from the carriers and I think they would be glad to respond.

You could totally eliminate the concept of the regulated airline-by-airline, point-by-point approach—the EAS service—and provide a flat subsidy per passenger generated which would encourage

them to create more service and generate more passengers. That would be a fairly substantial subsidy.

The EAS Program today only costs 1/200th of the costs of the Washington subway system. A final approach would be to apply total regulation as the Government does with military airlift contracts. Specify that this much service will be given to these cities over these routes, and allow the carriers to bid for them. Obviously, the low bidder who was qualified would get it, but it would ensure a reasonable level of service over the routes that ought to be served.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Beyer follows:]

AVMARK INC.
WORLDWIDE AVIATION MANAGEMENT SERVICE

REMARKS OF

MORTEN S. BEYER, PRESIDENT

AVMARK, INC.

SENATOR BAUCUS.

My name is Morten Beyer. I am a resident of Lolo, in Western Montana, and President of AVMARK, Inc., an aviation consulting firm with offices in Montana, Arlington, VA and London, England. I have been in the airline consulting business for more than 40 years.

In my remarks here today I want to focus briefly on the major structural changes which have occurred in the airline industry under deregulation, show briefly the impact that it has had on air service to small communities nationwide, and then concentrate on some of the direct effects it has had on Montana.

As shown on Chart 1, there has been a dramatic mortality rate in the industry since 1978, resulting in an increasing consolidation of airlines large and small:

- The eleven major airlines have shrunk to eight.
- The eight former local service carriers are now two, and they are trying to merge.

- The eight original low cost charter airlines have been reduced to one -- through bankruptcy and abandonment.
- Fourteen former regional airlines have shrunk to four.
- Over 100 new upstart airlines were certificated by the CAB. About 32 got "off the ground" but most have crashed, leaving only a handful still operating.
- Of the top 50 commuters in existence in 1978, 29 have disappeared, and others have risen to replace them.

Today, the top 50 carriers who constitute 90 percent of the commuter industry are captives of the major carriers, in part or in total owned, controlled and financed by the giant carriers and relegated to serving the big airlines at their hubs. Chart 2 presents typical examples of this feeder commuter service since 1978.

There has been a shift away from the smaller communities to the larger traffic generating points by the certificated route air carriers. Thus, by 1985, aircraft departures at the large and medium hubs increased by 29 percent over 1978. During this same period, aircraft departures at the small and non-hubs decreased by 31 percent. The impact of this service shift is seen in the respective traffic generation. At the large points passenger enplanements increased by 55 percent, while the smaller points showed a decline of four percent.

This shift away from smaller communities and the increasing captivity of commuters have had a catastrophic effect on air service in the United States. Chart 3 shows that 140 communities have lost all scheduled air service since 1978, and an additional 190 cities which used to receive service by the major and regional airlines now receive service only from commuters (Chart 4), and the vast bulk of this is solely to the nearest hub of their major masters. There is no question that the major hubs are receiving more service -- many would argue too much -- as more and more flights are jammed into the hubs, and fewer provide linear service to and between the smaller cities and communities.

And of course, if the essential air service program is dropped, as is scheduled, another 316 small communities face a loss or reduction of their remaining services as well.

Prior to deregulation 14 cities in Montana received scheduled air service by four airlines: Northwest, Western, Frontier and Air West. Montana has been relatively lucky -- no city has lost all service. But the quality has been seriously eroded in terms of aircraft type, size, and route patterns. Let's look at the picture:

In 1972 Montana's small Eastern cities received service from Frontier.

- One route ran along the High Line from Minot and Williston, ND to Great Falls via Wolf Point, Glasgow and Havre.
- Another route ran from Williston to Billings via Sydney, Glendive and Miles City. The seven small cities generated a total of 1,587 passenger in a typical 3rd Quarter.
- In the western part of the state a network of flights connected to seven larger cities, served with both jets and large turboprops.
- The seven larger cities generated 105,097 passengers in the same period.

Between 1972 and 1977 service to Western Montana improved greatly while Eastern Montana's service was altered to feed Billings, and the High Line service was discontinued. The overall effect on passengers in Eastern Montana was a more modest increase of 54 percent to 2,441.

But jet service to the rest of the state increased markedly, and business boomed. Bozeman traffic increased sevenfold, Helena, Missoula and Kalispell increased three or fourfold, and statewide traffic more than doubled.

In the last ten years, Frontier withdrew from Eastern Montana, to be replaced by Big Sky, who has tried valiantly to

maintain service despite the vagaries of the Essential Air Service program. It must be understood that the main objective of EAS is to provide the minimum level of service, with the smallest possible aircraft, to the fewest number of points. Thus the loss of service to 140 cities we mentioned earlier. In Montana it has meant that the 19-passenger pressurized Metros and Jet Streams previously used have been replaced with 9-passenger, one-pilot, piston-driven Cessna 402s. Where it cost $12.00 a passenger to subsidize Frontier ten years ago, it now costs $83.00 a passenger even for Big Sky's minimal service. In the last quarter, total boardings at the seven cities had fallen to 2,164 -- a drop of 12 percent in the decade.

In the West, Northwest also began a retrenchment of the intra-Montana services. Helena and Butte were turned over to Big Sky. Bozeman and Missoula lost jet service to the West -- Spokane and Seattle -- and now must depend on commuters. Total traffic from the seven Western Montana points declined ten percent from 223,000 to 201,000 passengers.

As shown on Chart 5, there was a close correlation between service (seats offered) and traffic generation. The extensive expansion of service before deregulation resulted in correspondingly increased passenger enplanements. After

deregulation however, the service reduction reflected in the depressed traffic results.

And horrible things also happened to fares in Montana's local markets. As seen on Chart 6, fares from Billings to the seven small cities of Montana increased 250 percent to 320 percent. You can fly coast-to-coast for $99, or to Europe, for less than it costs from Billings to Wolf Point.

Chart 1

CASUALTY RATE

AMONG CERTIFICATED AIR CARRIERS 1978–87

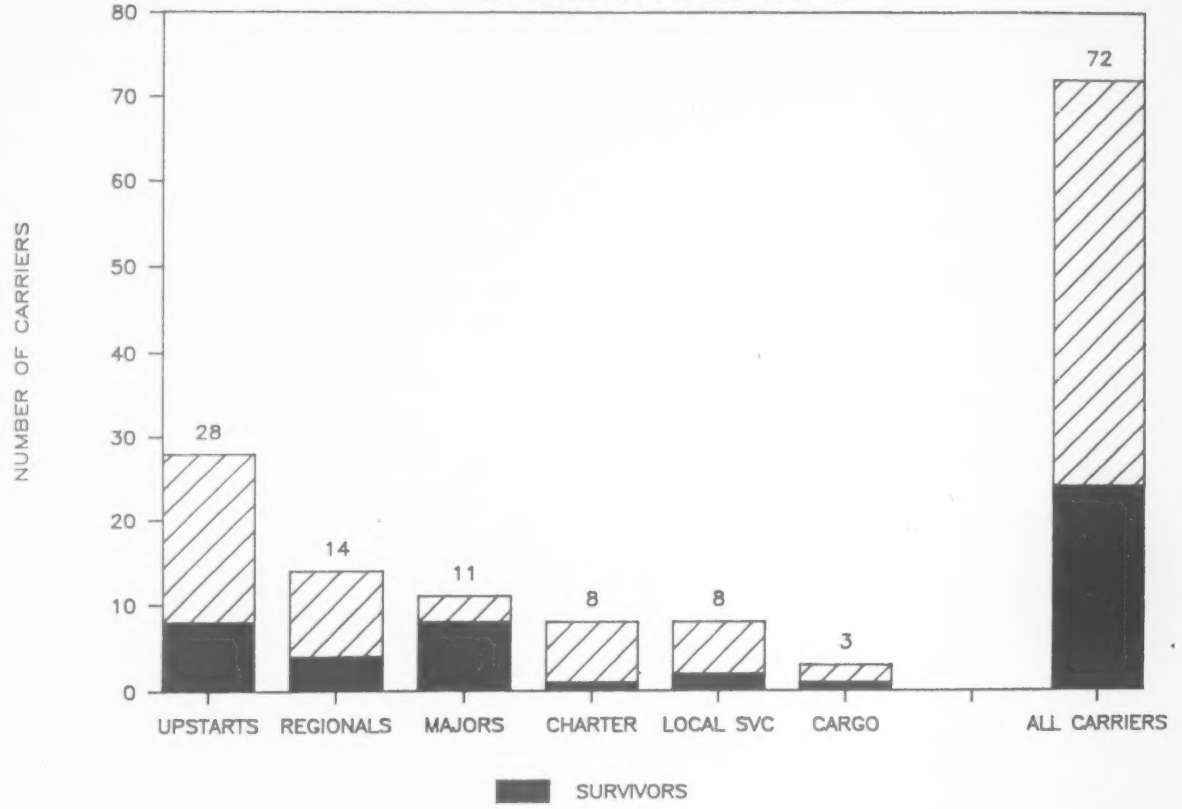

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Chart 2
Page 1 of 2

NORTHWEST AIRLINK

EXPRESS AIRLINES & MESABA

DELTA CONNECTION

Chart 3

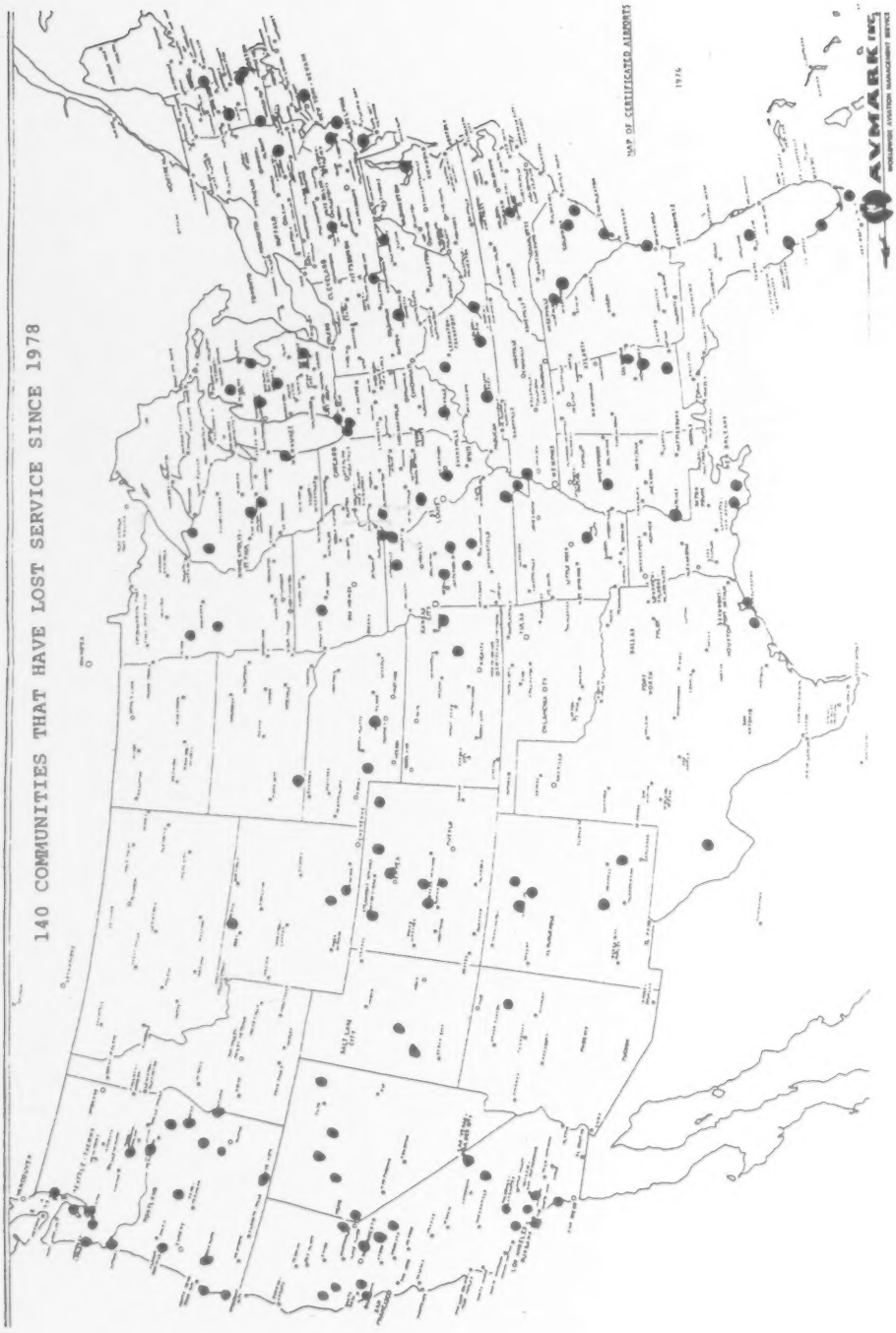
140 COMMUNITIES THAT HAVE LOST SERVICE SINCE 1978
MAP OF CERTIFICATED AIRPORTS
1976
AVMARK INC.

Chart 4

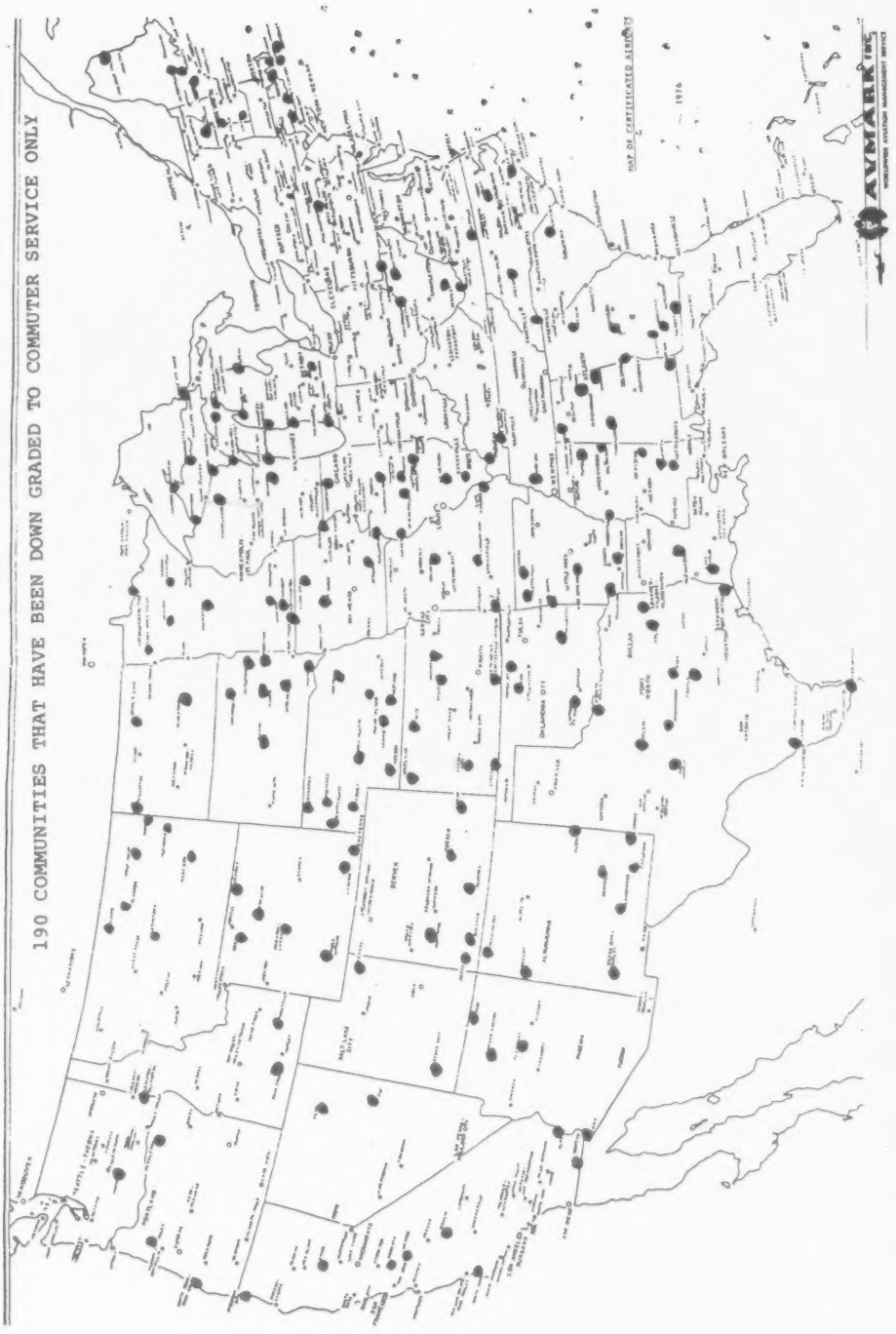
190 COMMUNITIES THAT HAVE BEEN DOWN GRADED TO COMMUTER SERVICE ONLY
MAP OF CERTIFICATED AIRPORTS
1976
AVMARK INC.
WORLDWIDE AVIATION MANAGEMENT SERVICES

Chart 5

MONTANA CITIES
CHANGES IN SEATS OFFERED AND TRAFFIC GENERATED
1972-1977-1985

Outbound From	Percent Change In Seats Offered 1972-77	Percent Change In Seats Offered 1977-85	Percent Change In Enplanements 1972-77	Percent Change In Enplanements 1977-85
Larger Points				
Billings	120	14	132	(14)
Bozeman	363	48	564	22
Butte	153	(71)	51	(55)
Great Falls	78	4	(1)	2
Helena	265	(34)	251	(21)
Kalispell	157	(10)	223	9
Missoula	938	32	346	27
Total	161	4	113	(5)
Smaller Points				
Glasgow	122	(54)	130	(60)
Glendive	26	(58)	65	1
Havre	(72)	73	5	58
Lewistown	(8)	16	25	(58)
Miles City	20	(33)	15	2
Sidney	14	105	60	69
Wolf Point	(9)	(17)	30	18
Total	13	(20)	64	(17)
Total State	151	4	112	(6)

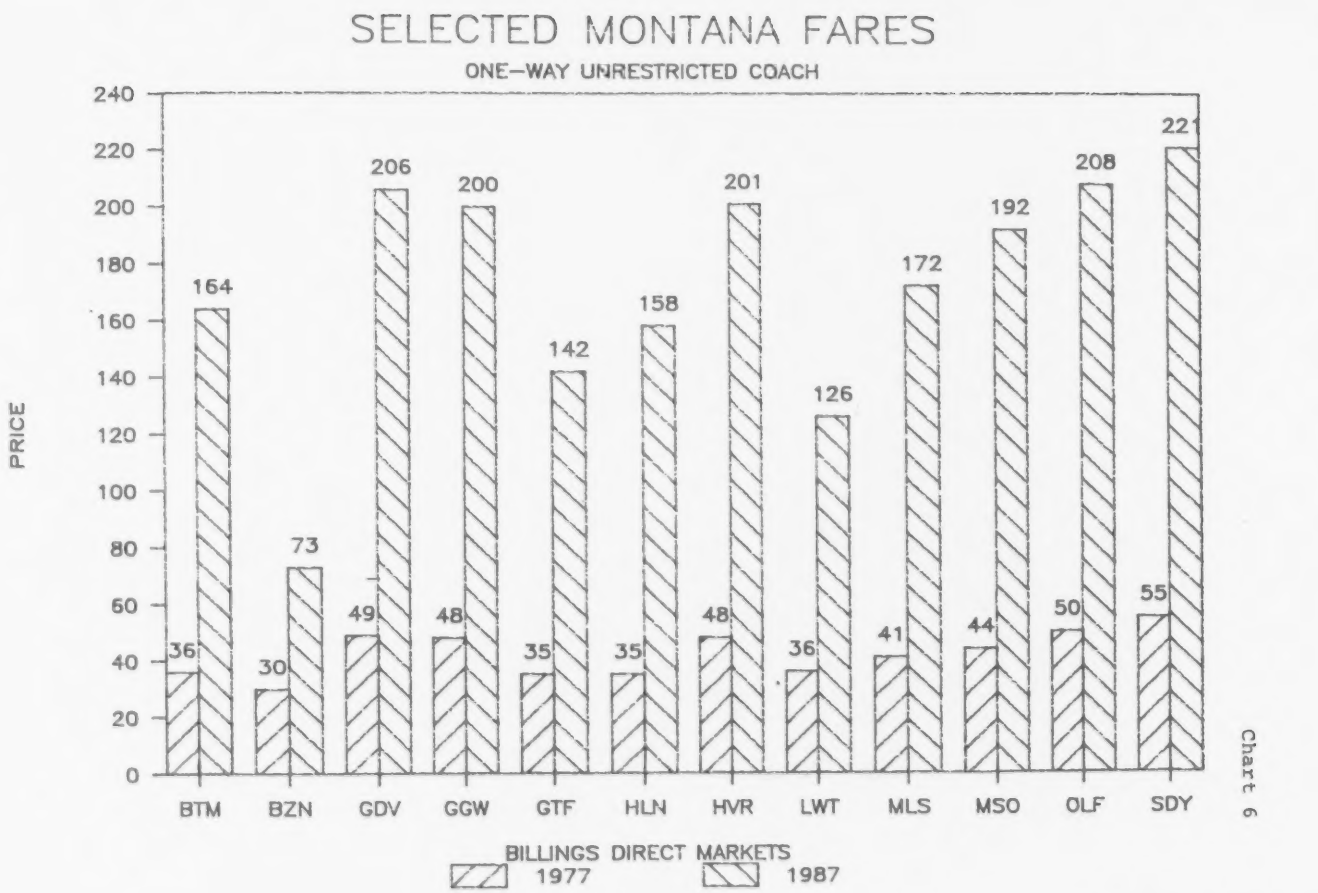

Chart 6

AVMARK INC

The CHAIRMAN. Thank you very much, Mr. Beyer.
Mr. Nance.

STATEMENT OF JOHN J. NANCE, WRITER/AUTHOR, TACOMA, WA

Mr. NANCE. Thank you, Mr. Chairman.

First of all, I would like very much to express my appreciation to the Committee and the Members of the Subcommittee for inviting my participation in what I consider a very vital and necessary inquiry.

My position from which to examine the questions before you is somewhat unique, in that it does not involve a stance of parochial advocacy. Rather, it stems from my research and involvement in the issues of human factors and aviation safety as an author-journalist over the past 4 years and my probes into the questions of deregulation's effects on various aspects of the airline industry, tempered by the reality of an insider's technical knowledge of the system and how it operates. And that results from many years as a commercial airline pilot and having been associated with this business for quite a few years prior to that.

Deregulation has resulted in two principal generic, and unavoidable I think, categories of adverse change in the air transportation system as it affects rural America: One is instability, both in the level of service and in the type of service; and two, is the substitution of inferior quality.

While there have been some notable exceptions among smaller communities, the 1987 reality from most rural areas is a bit like a hangover after a lengthy period of overindulgence. The morning after, in which too many towns and communities have awaken to find that their local air service has been diminished and quality or quantity or both, and that this free market deregulatory system in which airlines can come and go at will, is incapable generically of assuring them a stable level of airline service.

There has been a definite pattern discernable in rural America since 1978, in which airlines large and small established service to small towns with great hoopla, only to be forced by insufficient revenues and profits to quietly abandon the route or to go bankrupt within a year or so.

While this may seem wonderful to those who love from afar the rough and tumble atmosphere of unfettered free enterprise, there are serious societal prices to be paid for this type of disruption, and those prices are being paid, and have been paid literally and figuratively, by Americans who have had the "misfortune" to live outside of major population centers or airline hubs. That is not as it should be.

Simple municipal planning is a substantial victim. Airport funding, for instance, is often predicated on user fees, rents, and lease payments generated by the airlines large and small. Many times the establishment of a small commuter or regional airline comes about only after the municipal authority agrees to cooperate and even participate financially by providing new and expensive airport facilities through bond programs or contractual arrangements which make the community indirectly a financial hostage to the success of that carrier.

If, however, there are suddenly no users because of unsubsidized air service being abandoned or reduced, the entire foundation of planning on which brave financial municipal decisions have been made may be washed away overnight, and often are.

New terminal buildings suddenly may be left empty with no one to pay the rents that were anticipated, and there will be no one to provide passenger service flow which justified the project to begin with. As one airport manager in the State of Washington told me just last week, he said, "we cannot count on anything from these airlines. They will not commit to a lease without a blanket escape clause, which makes the lease useless, and basically, they will not commit to anything."

The economic health of an entire region can be imperiled by the loss of air service; its image and ability to attract new capital often depend on being part of mainstream America which requires, in this day and age, consistent airline service not only for the movement of people but also for baggage and freight.

Yet, under deregulation, over 101 non-EAS cities have lost all service and we have other people giving figures today, such as Mr. Beyer. Many more cities have been buffeted by on again off again schedules and airlines which have gone through a nightmare of uncertainty.

In addition, rural America seems to be asked to pay the bill on low density routes. For $99 coast-to-coast fares, for instance on high density routes, this a, "borrow from Peter to pay for Paul's fare" syndrome in which the poor passenger from Dubuque to Chicago pays $1 per seat-mile which the passenger from L.A. to New York gets by for 3.3 cents per seat mile. Peter, of course, in that analogy, is rural America, and he has been getting mugged throughout this process.

The second major category—and this is a very serious one—is the substitution of inferior airline service for the level the larger carriers could provide. This means the substitution under deregulatory freedoms of commuter/regional carriers which cannot rise to the same leaves of safety, comfort, reliability, speed, aircrew qualification, or operational stability as the major and intermediate carriers which they, in too many cases, replaced.

There are a few the exceptions—a few major commuter regionals, which are almost indistinguishable in their operations from the majors—who operate almost exclusively under part 121.

But the majority of commuter regional airlines cannot provide the same level of service or safety as the major or intermediate part 121 air carriers. This is a generic difference.

The aircraft they fly are usually less sophisticated, less well equipped, largely unpressurized, and much smaller than mainstream jetliners. Many are devoid of not only restrooms, they are also devoid of radar, devoid of decent cockpit communications, devoid of sophisticated flight instruments, devoid of those elements that are part of the safety buffer which all of us as Americans have come to expect of our air transportation system, whether we are boarding in a rural area or not.

In addition many of these aircraft, most of them in fact, fly at altitudes most vulnerable to weather hazards and potential mid-air collisions. They are maintained by less sophisticated maintenance

departments, they are flown by less experienced pilots, usually in the first airline job of their career. Finally, such airlines are often owned—too often, I might add—and operated by good American entrepreneurs who at the same time, unfortunately, carry into the business a lack of sophistication of technical knowledge of the aviation business and who can too easily encourage marginal or unsafe operations by managing what is essentially a delicately-balanced human system as if it were something like a truck assembly factory.

This is the type of carrier which has been handed to rural America as an adequate substitute for the major and intermediate airlines which existed and served the public prior to 1978, and this is the substitute which regardless of good intentions—and this field is awash with good intentions—cannot rise to the standards expected of it.

Those people boarding such flights, whether coming from rural America or going to it, have been told wrongly especially with these sharing agreements that the level of safety that they will find on the small airplane is equal to what they just left. In fact, many times they are not even told that it is a small airplane until they have rounded the corner with their major airline ticket.

This is just a capsuled glimpse of the problem, and I hope that you will examine my more lengthy statement for the record.

Once again, I thank you Senator, for your invitation to appear.

[The prepared statement of Mr. Nance follows:]

Testimony of John J. Nance, Writer/Author, before the Subcommittee on the Rural Economy and Family Farm of the Senate Committee on Small Business, presented October 28, 1987.

First I would like to express my appreciation to the members of the Subcommittee for inviting my participation in this very vital, and very necessary inquiry. My position from which to examine the questions before you is somewhat unique, in that it does not involve a stance of parochial advocacy. Rather, it stems from my research and involvement in the issues of human factors and aviation safety as an author-journalist over the past four years and my probes into the questions of deregulation's effect on various aspects of the airline industry, tempered by the reality of an insider's technical knowledge of how this system really operates - a knowledge which results from over 12 years of participation as an aircrew member, including nearly 9 years with several commercial airlines. In addition, I think my views reflect those of tens of thousands of professional airline people (as well as fellow citizens unconnected with the airline industry) in affirming the importance and urgency of your inquiry, and the urgency of other similar hearings on Capitol Hill which are looking for ways to repair and revitalize a critically important element of our national life: the air transportation system of the United States. We have been engaged during the past 9 years in an experiment with free market forces unleashed on a vital, national public utility. We have seen some benefits to the American people from this experiment, yet this system has experienced great unexpected damage as a result of this experiment - damage to stability, damage to service, damage to operational philosophies and perceptions, damage to vital elements of governmental control, damage to lives and careers, damage to the growth of communities across the nation, and damage to the safety buffer which, during the 40 years of development of our airline system up to 1978, had enabled us to build an incredibly safe and reliable means of national airborne transportation. Given these facts - and they are indeed facts - it seems obvious that careful, balanced, and honest recognition of the faults of our national deregulatory experiment in the airline business is long overdue. It should also be pointed out, however, that the process of finding and curing such faults does not, of necessity, threaten any damage to good and beneficial elements of competition within the industry. Extremism or ideological purism in a pluralistic society seldom if ever serves the society as a whole, and this is as true of an extremist economic theory as it is of a political philosophy. The idea that we must chose between either full deregulation with zero governmental control over routes, rates, and fitness of carriers, or in the alternative, full dictatorial regulation, is simplistic and naive. The truth is, we can have a balance between them - a system invigorated by the natural forces of

competition kept within the confines of responsible public service by aggressive governmental oversight applied only where needed.

More to the point of your specific inquiry, the negative effects of deregulation have been very pronounced in rural America - and the outcries of concern from rural America have been largely ignored.

Deregulation has resulted in two principal, generic, and unavoidable categories of adverse change in the air transportation system as it affects rural America:

1. Instability; and,
2. Substitution of inferior quality.

From these two categories flow a host of problematic effects never reflected in the inaccurate assurances of deregulatory purists that deregulation has provided unlimited benefits to the public. In fact, the "benefits" that have resulted are simply an increase in overall passenger traffic nationwide (much of which would have occurred anyway through economic and population growth), and the presence of generally lowered fare structures, usually limited to airline routes transiting major city-pairs or markets which have been subjected to intense competitive fare wars. For the most part, temporarily lowered fares are seldom available to those unfortunate enough to live outside the major U.S. population centers, or those who cannot plan weeks in advance and confine their travels to major carrier groups and co-shared reservation listed airlines. Therefore, when this entity called "the American public" is cited as a beneficiary of deregulation, you should be aware that the specific "public" being referred to is, in fact, a very limited group of our citizenry. While there have been notable exceptions - small communities which have enjoyed a cornucopia of choice in airline service due to the increase in traffic and the number of regional airline companies - the 1987 reality for most rural areas is a bit like a hangover after a lengthy period of overindulgence. In this "morning after", too many towns and communities have awakened to find that their local air service has been diminished in quantity or quality, or both; and, that this free-market deregulatory system in which airlines can come and go at will is incapable of assuring them a stable level of airline service. In fact, the celebrated deregulatory freedoms to go bankrupt or to abandon rural airports at will are utilized with a vengeance by too many regional airline owners who, unlike the traditional airlines of the past, are more dedicated to profit than to community service and the building of an air transportation system.

INSTABILITY

Now, specifically, let me address the problems created by lack of stability in the rural extents of the airline system.

The first problem is the negative effect of the growth and development and the economic health of rural communities created by the unpredictability inherent in a deregulatory system.

In order for a small town or community in our nation - whether in the east or the west - to attract a wide variety of new businesses (especially high-tech manufacturing concerns), attract tourism, keep existing industry (especially those dependent on air transportation), maintain a sound capital base or attract new capital, and maintain the image of a vibrant, growing community in the mainstream of American life which is so necessary to many other facets of municipal growth and success, scheduled airline service is vital. Highways and Amtrak are not enough to bring a community sufficiently into the mainstream.

This means that adequate, financially-stable airports are vital in any such community - airports with sufficiently modern facilities and sufficient space to permit the operation of the latest turboprop or turbojet aircraft. In order for small communities to take the brave step of initiating the bond issues and other financial or contractual arrangements necessary to build and maintain such airports, rural communities have to depend on the fact that the airline service will be there in the long term, without fail, to pay the bills and attract the passenger cash-flow to service the debts.

But this becomes almost a Catch-22. To attract airline service, the community must provide the fixed-base support for that airline service, yet to provide that support, investment and contractual arrangements (exposing rural communities to substantial debt) wholly dependent on the retention of airline service are necessary. Thus the most vital element in the rural airline equation is stability - and that means the ability of the rural community to depend on continuous air service from a carrier of sufficient financial stability to provide stable schedules, decent equipment, high levels of safety, and a substantial degree of commitment on the part of airline management to the development of long-term airline-community relationships.

Deregulation, however, has promoted exactly the opposite: instability. In too many cases, the smaller airlines which have come into being to serve smaller communities have been conceived on a shoestring, monitored insufficiently by an overwhelmed FAA, yet subsidized indirectly by community airport expenditures as they lurch into being as, essentially, a free-market gamble. If it were the case that such carriers normally became permanent fixtures and survived, this rocky process would be more tolerable. However, in far too many instances over the past 8 years, such carriers have failed and shut down (or in some cases been grounded by the FAA), leaving communities without service (or with a sharply reduced levels of service). Even in the absence of outright failure, the difficulty of making a profit as a commuter in the midst of a deregulated free-for-all will often lead management to make massive changes in the route structure, and such changes can include abandonment of one

or more of their original service cities as more lucrative routes beckon. And, as occurred almost immediately with the 1978 passage of the airline deregulation bill, large carriers continue to pull modern jet equipment and highly-trained personnel out of rural areas that cannot generate enough traffic to support the big carrier, and the swarm of on-again, off-again commuter carriers who siphon the existing traffic from the big carrier.

Before anyone accepts the incorrect concept that deregulation has resulted in no cutbacks in rural air service, let's look at the facts: Among the non-essential air service markets which do not receive a subsidy, 101 American communities have lost all scheduled air service between June of 1978, and June of 1987. In the same period weekly departures in non-essential service cities has decreased a staggering 44.7%, despite the constant influx of new commuter carriers which, for the past seven years, have been rotating in and out of business with great sound and fury signifying confusion. While essential air service cities have seen an 8.7% increase in subsidized weekly departures, even the subsidies have not prevented erosion: the number of seats available each week has declined 17% in the same measurement period.

But even more important than the outright abandonment or reduction of air service is the unpredictability of the service - the instability of the system. The reality, in other words, is that smaller communities have been faced with great, continuous turbulence in which airlines are serving their airports at any given time, how many flights come and go, and at what times, and for how much.

There has been a definite pattern discernable in rural America since 1978 - a pattern in which airlines large and small establish service to small towns with great hoopla, only to be forced by insufficient revenues and profits to quietly abandon the route - or go bankrupt - within a year or so. While this may seem wonderful to those who love from afar the rough and tumble atmosphere of unfettered free enterprise, there are serious societal prices to be paid for such disruption, turbulence, and uncertainty - and those prices are being paid - literally and figuratively - by Americans who have the "misfortune" to live outside of major population centers or hubs.

Simple municipal planning is a substantial victim. Airport funding, for instance, is often predicated on user fees, rents, and lease payments generated (if not paid directly) by airlines large and small serving a community. Many times the establishment of a small commuter/regional airline comes about only after the municipal authority agrees to cooperate and even participate financially by providing new and expensive airport facilities through bond programs or contractual arrangements which make the community indirectly a financial hostage to the success of the carrier.

If, however, there are suddenly no users because unsubsidized air service is suddenly abandoned or severely reduced (for reasons over which the locality has virtually no control), the entire foundation of planning on which brave municipal financial

decisions were made may be washed away. New terminal buildings suddenly may be left empty with no one to pay the rents that were anticipated, and there will be no one to provide the passenger flow (not to mention local cash flow) which justified the project to begin with. As one airport manager told me just last week, "We can't count on anything from these airlines. They won't commit to a lease without a blanket escape clause, which makes the lease useless, and basically they won't commit to anything. Yet they want all your counter space and support and services, and they want them now. So we go through all the gyrations, and then they suddenly pull out. It's terrible."

My experience and research in this area - and travels throughout the country - have convinced me that there is a serious retardant effect flowing from such instability, and that the situation must be changed if we are to expand, not contract, our air transportation system. Airport authorities, city fathers, and county officials must be able to have confidence in a continued level of air service when they put their professional and political necks on the line in saddling their population with new bond projects, new taxes, or simply new agreements which might prove very costly if their local air carrier leaves them without service.

Certainly a greater level of service stability and assurance is needed if rural America is to be a full participatory partner in our national transportation system. And since rural Americans certainly pay their share of the taxes used to establish and maintain our federal subsidy of the air traffic control system, the FAA, and the Department of Transportation, I believe all of us would agree that where possible and practical, the rural population of the nation has a right to expect federal support for, and assurance of, a usable level of service from that system. This is not being provided by today's free market system, nor can it be provided with any degree of assurance and continuity. And, again, it is that need for assurance of continuity and stability that is a vital element in the economic growth of any rural area attempting to attract new business concerns.

It is also important, I think, for the airline industry to stop subsidizing ridiculous below-cost fares between major city pairs by grossly overcharging passengers who originate in smaller, less profitable markets, or who want to fly to such small towns. The "borrow from Peter to pay for Paul" syndrome has been one of the unfortunate truths of airline pricing during the deregulatory wars of the past few years, a syndrome in which the poor passenger from Dubuque to Chicago pays a dollar per seat mile while the passenger from Los Angeles to New York gets by for 3.3 cents per seat mile. In that example, of course, "Peter" is rural America, and he's getting mugged.

In many cases the fares in rural markets have doubled or tripled over the past year-and-a-half as deregulation continues to die a painful death at the hands of growing oligopoly - the mergers and progressive creation of mega-carriers consisting of major airlines owning, operating, or controlling a growing spider-web of

feeder, regional/commuter airlines. Before dismissing the warning that this process will continue and will remain unresponsive to the needs of anything but the bottom lines of major airline companies, a review of the ignored opposition testimony before both houses of Congress in 1978 would be appropriate. Witness after witness warned that what is happening, would happen, and in fact would be an inevitable result following perhaps as much as a decade of decay in local air service. Those warnings were correct.

Finally, it is very clear from our recent history that a situation in which five major air carriers attempt to serve a mainstream city-pair whose passenger base can only support three carriers, leads inevitably to severe economic difficulties for all the carriers involved. Cost-cutting frenzies by all, and eventual market-abandonment by one or more of the competitors, is the ultimate result. In small, rural markets, however, the small airlines which pop up or extend their route systems to new communities do not have the financial staying power to engage in lengthy fare wars and service wars. When challenged, they must win fast or get out. The result is too often a quick abandonment of airline service to a rural community, and some poor airport manager left with a nightmare of unpaid rents, unoccupied counters, and unfulfilled leases. The Congress should, I believe, find ways of preventing the number of airlines competing in a rural market from exceeding the passenger base. True, that means some form of economic re-regulation, but there is no escape from the fact that the alternative - leaving the problem to the free market - causes massive disruption for extended periods of time, and may never be able to provide a stable level of airline service for hundreds of American communities.

SUBSTITUTION OF INFERIOR SERVICE

The second major problem category is the substitution of inferior airline service for the level the larger carriers could provide. This means the substitution under deregulatory freedoms of commuter/regional carriers which cannot rise to the same levels of safety, comfort, reliability, speed, aircrew qualification, or operational stability as the major and intermediate carriers which they, in too many cases, replaced.

I could engage in a very lengthy dissertation involving all manners of example of the differences between regional/commuter carriers and major air carriers, but I will keep this very brief. Suffice it to say that with the exception of a very few major commuter/regional airlines who operate almost exclusively under Part 121 of the Federal Air Regulations, the vast majority of commuter/regional airlines cannot provide the same level of service or safety as major or intermediate Part 121 air carriers.

This is a generic difference. The aircraft they fly are most often less sophisticated, less well-equipped, and often foreign-built mini-airliners whose certification has in many cases been largely outside the control of the FAA. The commuter/regional

fleet is largely unpressurized, and often subject to much higher cabin-noise levels than mainstream jetliners. Many are devoid of restrooms, devoid of radar, devoid of descent cockpit communications, devoid of sophisticated flight instruments, and devoid of those elements of the safety buffer which Americans have come to expect of their air transportation system. In addition most of these aircraft - due to lack of cabin pressurization and the short stage lengths of their flight operations - fly at altitudes most vulnerable to weather hazards and potential mid-air collisions with uncontrolled traffic. The aircraft are often maintained by far less sophisticated maintenance departments and mechanics than the major carriers, and are flown by pilots who, for the most part, are very young and inexperienced and operating in the first few years of their aviation career. The vast majority of such pilots rotate within a year to the major carriers, who themselves have been experiencing an increasing shortage of qualified pilots - a siphoning effect which promises to get far worse in the years ahead. Finally, these carriers are often owned and too often operated by entrepreneurs who are unsophisticated in the technical side of airline operations, and who can too easily encourage marginal or unsafe operations by managing what is essentially a delicately-balanced human system as if it were a truck assembly factory. Then too, because of very limited financial resources, flight training is usually kept to a bare minimum, maintenance is often treated the same way, and there are few flight departments or other professionally-staffed, technologically-sophisticated groups of people within commuters who can properly answer the constant technical questions and help make the sensitive and important safety decisions about what is flyable and what is not. Too often - and my research confirms this on a weekly basis - flight crew members are pressured directly or indirectly to fly marginally-safe aircraft they do not feel right about flying, or encouraged subtly or directly to launch into weather conditions that they do not feel are conducive to maximum safety. When the bottom line is made the arbiter of safety decisions - as becomes inevitable in marginally-financed operations - the question becomes "How much safety can we afford?" rather than the traditional question of "How much safety is enough?"

While I truly believe that the vast majority of commuter/regional airlines are owned and run by honest people who have no desire to provide any lower level of service or safety than the major carriers, the truth of the matter is that there is a substantial difference between commuter/regionals and the major carriers (except, as previously mentioned, for the largest of the regionals).

Now, this is the type of carrier which has been handed to rural America as an adequate substitute for the major and intermediate airlines which existed and served the public prior to 1978. This is the substitute which regardless of good intentions, cannot rise to the standards expected of it. This is the type of airline which tens of thousands of Americans confront when they round

the corner of an air terminal, having just alighted from a Boeing or a Douglas jetliner on the ticket of a major carrier, to discover that their connecting flight is on a Twin Otter, or a Beechcraft 99, or a Piper Seneca, or some foreign-built commuter turboprop, each of them bearing the name of the major carrier along with a qualifying word such as "commuter" or "express". And, these are the passengers, whether coming from rural America or going to it, who have been told wrongly that the level of safety they will find on that small airplane is equal to what they just left.

Again, let me not give you the impression that I feel commuter/regional aviation is unsafe by definition, or unworthy of certification as a class. The vast majority try hard. It is simply an irrefutable fact that the level of safety - and the level of service in terms of cabin size, cargo holds, operational reliability and so on - cannot rise to the same levels as mainstream Part 121 airlines.

Now, commuters certainly existed in rural America prior to deregulation, and they were far worse as a class in terms of safety than they are today. The problem is that they, as a class, have been brought into the mainstream of America's airline system, passed off to the public as a one-to-one equivalent, and handed to rural America as a replacement for Part 121, major carrier service, and this is not conducive to the goal of improving and expanding our national air transportation system. While there will always be a role for the small airline, their standards - if they are to be a part of the main system - must be brought up to that of the Part 121, mainstream carriers. I would suggest that Congress realize that this substitution of dissimilar quality has been an inadvertent fraud on the flying public, and move to require the abolishment of Part 135 operational rules where scheduled passenger operations are concerned. Yes, this is harsh. Yes, this would probably require subsidies again to maintain air service following the collapse or withdrawl of tiny carriers who could not afford to upgrade their equipment, their standards, and their operations. But having been in the middle of this problem for many years now, I must say I am totally convinced that airlines and Part 135 standards do not mix.

Finally, I would point out that even though the FAA has tried very hard to monitor airlines, the record - and their own studies of past years - has shown categorically that when there is massive turbulence in the entry and exit, the start-up and collapse of commuter/regional air carriers, the FAA simply cannot monitor them. Therefore, the category of airline that most needed monitoring and strict FAA supervision because of their thin financial margins, thin experience levels, and limited technical resources during the chaos of the past decade, have been the least-controlled by FAA personnel. That must be changed, and I submit to you that though it touches an ancillary hearing record of another committee, strong congressional support for immediate removal of the FAA from the DOT and immediate exponential increases in budget, scope of authority, and internal structure are a vital national priority which soars several flight levels above Graham-Rudman if we are to even catch up to 1987 - let alone face the 90's and the next century.

The CHAIRMAN. Thank you, Mr. Nance.
Mr. Dempsey.

STATEMENT OF PAUL STEPHEN DEMPSEY, PROFESSOR OF LAW AND DIRECTOR, TRANSPORTATION LAW PROGRAM, UNIVERSITY OF DENVER COLLEGE OF LAW, DENVER, CO

Mr. DEMPSEY. Mr. Chairman, my name is Paul Stephen Dempsey. I am professor of law and director of the Transportation Law Program at the University of Denver. It is a great honor to be invited to talk to you about one of the most significant issues facing the country. That is the impact of a major shift in regulatory policy upon users of an important infrastructure industry.

I want to talk about costs and benefits—mostly the costs—because other commentators have explored benefits quite adequately—and the winners and losers of this major change in governmental policy.

It seems to me that there have been five major costs of airline deregulation, the first being concentration. We have ended up with an industry which is an oligopoly of mega-carriers. The top five airlines in the United States today control 72 percent of the market. In January 1986, they were responsible for only 54 percent of the market.

There is particularly egregious concentration at the major hubs, including Minneapolis/St. Paul and St. Louis, where a single airline in each city controls more than 80 percent of the gates, 80 percent of the landings and take offs, and 80 percent of the passengers.

Second, there appears to have been a significant deterioration in the margin of safety since deregulation began. Near-misses are soaring, aircraft maintenance seems to be deteriorating and the Department of Transportation has been lethargic in restaffing air traffic controlled towers to their pre-PATCO strike levels.

Third, a drastic deterioration in labor/management relations has occurred. Although labor costs have been held down, there has been a social price which has been paid.

Fourth, consumer abuses exist nationwide. False and misleading advertising, deliberate overbooking, and unrealistic scheduling all are serious problems.

Fifth, and the one that we are going to talk about here in great detail, I hope, is particularly poor service and higher prices for small communities, in terms of abandonments, service curtailments, and discriminatory pricing.

There are winners and losers under deregulation. The beneficiaries under deregulation are the larger users of the system—large companies, large communities. The losers are small businesses, small towns and rural communities. That is true beyond airline deregulation. It is also true for bus deregulation; 4,500 small towns have lost service since bus deregulation began, while and only 900 have gained it.

For railroad deregulation, we have a little more than 200 passenger trains in the United States. In 1929 we had 20,000. There have been 1,200 railroad abandonments since the promulgation of the Staggers Rail Act of 1980. Discriminatory pricing in the trucking

industry is a particular problem for small towns and small shippers.

Beyond transportation local telecommunications rates are up between 38 and 52 percent for local residential users, while they have gone down to a lesser extent for a long distance. In banking, higher interest rates for small towns are going up. Electric utilities, if they are deregulated, will impose their fixed—cost burden on smaller users and local residential customers as has occurred in the other deregulated industries.

Before deregulation we had a system of cross-subsidy, whereby carriers had a common carrier responsibility to take revenues that they were earning in lucrative markets and cross-subsidize less than adequate profits that they were earning in small communities. That cross-subsidy has reversed in direction. Today the fixed cost burden is being borne by local users of every deregulated infrastructure industry.

The Airline Deregulation Act of 1978 was designed to ameliorate some of that adverse impact upon small communities by creation of the Section 419 program of essential air transportation services for 10 years. In fact, it was anticipated by the Kennedy subcommittee that there would not be a significant disruption of service for small communities. But these projections were spurious. Indeed, during the first 2 years of deregulation there was rather a severe disruption.

Prior to deregulation, fewer than 10 communities a year lost service. In the first 2 years of deregulation, more than 50 communities lost all their transportation services. Since deregulation has occurred, 225 airports have suffered more than a 50 percent decline in available seats; approximately 120 airports have lost all their services. Some consumers complain about smaller, unpressurized aircraft. There are, indeed, less comfortable. They are also decidedly less safe.

Depending upon how it is measured, commuter airlines flying propeller driven aircraft have between a 3 and 37 times worse safety record than do scheduled airlines flying jet aircraft. There has also been a problem in terms of circuitous routing. If you travel from Cheyenne to Casper, you must go through Denver. You cannot fly directly through Wyoming.

Ticket prices have increased disproportionately for smaller users of the system to small communities. I wrote a piece in Newsweek in the "My Turn" column about 2 weeks ago, in which I pointed out that the airfare from Madison, WI, to St. Louis is higher than the airfare on TWA from New York to Los Angeles via St. Louis.

Prices, I think, are reflecting the level of competition in markets and not the marginal costs of operation. The real affects of deregulation upon small communities will be felt if the section 419 subsidies are eliminated. A survey of the Fortune 500 top companies reveals that 80 percent of them would not locate in a city which did not have reasonably adequate air transportation services. The impact will ripple perniciously throughout the economies of the approximately 150 communities which will lose service if the subsidies are discontinued.

It is, I think, a great paradox that people who live in rural communities are those most philosophically opposed to Government

control. Nonetheless, these are the people who are suffering most under deregulation than any other sector of our economy.

Thank you, Senator.

[The prepared statement of Mr. Dempsey follows:]

BEFORE THE SENATE COMMITTEE ON SMALL BUSINESS

HEARINGS ON THE IMPACT OF TRANSPORTATION DEREGULATION

ON SERVICE TO SMALL TOWNS AND RURAL COMMUNITIES

Washington, D.C.

October 28, 1987

STATEMENT OF

PAUL STEPHEN DEMPSEY*

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* Professor of Law and Director of the Transportation Law Program, University of Denver College of Law. A.B.J. (1972), J.D. (1975), University of Georgia; LL.M. (1978) George Washington University; D.C.L. (1986), Institute of Air & Space Law, McGill University. The author formerly served as an attorney with the Interstate Commerce Commission (1975-77, and 1981-82), and Civil Aeronautics Board (1977-79). He is a member of the Bars of the District of Columbia, and the States of Colorado and Georgia.

Note: An adapted version of this testimony will be published as a law review article, "The Dark Side of Deregulation: Its Impact on Small Communities", in volume 39 of the American Bar Association's Administrative Law Review (1987).

EXECUTIVE SUMMARY

1. In earlier periods of American history, Congress expressed a strong concern that small towns and rural communities have adequate and non-discriminatory access to the transportation network. In part, this public policy objective motivated both the federal and state governments to establish a comprehensive scheme of economic regulation for the infrastructure industries.

2. More recently, Congress has embraced competition, rather than regulation, as a means of accomplishing social ends. Federal legislation partially preempting state jurisdiction over entry and exit in the rail, air and bus industries was promulgated in 1958, 1978, and 1982, respectively.

3. Unlimited entry led to increased competition in the most lucrative markets, thereby squeezing carrier profits and making it difficult for them to cross-subsidize losses incurred in providing passenger service to small towns and rural communities.

4. Although deregulation has been implemented at different times, and utilized different statutory approaches, the net result has been nearly identical for all three industries. Rail, air and bus carriers have sharply reduced passenger service to America's small towns and rural communities.

5. After the 1958 federal rail legislation, 60% of America's passenger trains were discontinued. In 1970, Congress responded to this rapid deterioration of intercity rail passenger service by establishing Amtrak, a federally-subsidized company which today serves 500 communities, many of which have no alternative means of public transport. Reagan Administration budget proposals have called for elimination of Amtrak subsidies.

6. Airline discontinuances averaged 9.6 per year before the 1978 airline deregulation legislation, and more than 50 per year during its first two years. A subsidy program has made it possible for small, commuter airlines to replace service lost in 150 communities by the departure of the larger carriers. But passengers in small communities have nevertheless experienced a qualitative and quantitative deterioration in service, and higher rates. Moreover, federal subsidies will end in 1988.

7. Since bus deregulation in 1982, 4,514 communities have lost service, while only 896 have gained it. Many are left with no alternative means of public transport.

8. In addition to the social burden service deterioration places upon the poor and elderly, the loss of public transportation makes it extremely difficult for small towns and rural communities to attract new business investment, or indeed, dissuade existing businesses from leaving. Inevitably, this leads to a downward economic spiral, and an outmigration of youth.

I. INTRODUCTION

In recent years, Congress has promulgated major legislation designed to reform the regulatory environment for the passenger transportation industry. These statutes include the Airline Deregulation Act of 1978, and the Bus Regulatory Reform Act of 1982.1 Almost two decades before these legislative measures of relatively recent vintage, Congress enacted the Transportation Act of 1958, which significantly liberalized the ability of railroads to respond to market forces, and discontinue passenger service.

This comprehensive legislative agenda, coupled with the Presidential appointment of individuals fervently dedicated to market theory to head the regulatory agencies (i.e., the Interstate Commerce Commission [ICC], the Civil Aeronautics Board [CAB], and the Department of Transportation [DOT]), has meant that deregulation has swept through this industry rather more comprehensively than it would have had less ideological agency heads been in charge of its implementation.2

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1 Other such transportation deregulation legislation involving the movement of freight, as opposed to passengers, includes the Railroad Revitalization and Regulatory Reform Act of 1976, the Air Cargo Deregulation Act of 1977, the Staggers Rail Act of 1980, the Household Goods Transportation Act of 1980, the Motor Carrier Act of 1980, and the Freight Forwarder Deregulation Act of 1986.

2 See Dempsey, The Interstate Commerce Commission: Disintegration of An American Legal Institution, 34 AM. U. L. REV. 1 (1984) [hereinafter cited as ICC Disintegration]; Dempsey, Congressional Intent and Agency Discretion - Never the Twain Shall Meet: The Motor Carrier Act of 1980, 58 CHI. KENT L. REV. 1 (1982); and Dempsey, The Rise and Fall of the Civil Aeronautics Board - Opening Wide the Floodgates of Entry, 11 TRANSP. L. J. 91 (1979) [hereinafter cited as Rise and Fall of the CAB].

Any responsible effort to develop prudent public policy with respect to an industry as important to the nation's economy as transportation must attempt objectively to assess the costs and benefits of the new legislative environment. Various forms of deregulation have had now about a decade to run their course (and rail passenger liberalization has had three). It would seem, then, to be an appropriate time to reflect on the impact of deregulation, not only upon the industries which have been deregulated, but also upon those members of the traveling public who rely upon their services. Unfortunately, the literature criticizing the previous regime of regulation, and applauding the benefits of deregulation, tends to gloss over one of deregulation's major costs -- its impact upon individuals who reside in America's small towns and rural communities.3

Admittedly, the impact upon these constituencies has varied depending upon the mode of transportation involved. In part, these differences reflect the inherent characteristics of each mode, and the extent to which each has been deregulated.4 For these reasons, this analysis will segregate its findings among the several modes --

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3 See e.g., Hardaway, Transportation Deregulation (1976-1984): Turning the Tide, 14 TRANSP. L. J. 101, 106 n. 17 (1986), and articles cited therein. See also, S. BREYER, REGULATION AND ITS REFORM (1984).

4 For example, railroads, being tied to their track, are the least flexible of the several modes; airlines are addicted to airports; bus companies are far more flexible in their service capabilities, rolling over asphalt and concrete wherever poured. From an economic perspective, railroads have the highest fixed costs, and buses the lowest. The buses are the most fuel efficient mode for short distances, and the railroads for long.

railroads, airlines and and bus companies -- and in that order, since that is the order in which passenger service has been deregulated.

Modes of transportation are defined by statute as "common carriers", which have long been regulated at both the federal and state levels.5 They have traditionally had common carrier6 obligations imposed upon them, to serve all within their operating territories in a nondiscriminatory fashion in terms of both service and pricing.7 Industry spokesmen repeatedly warned that deregulating entry would lead to "cream-skimming", with competitors attracted to their most lucrative markets like sharks to the smell of blood.8 This would undermine one of economic regulation's most important objectives -- that companies cross-subsidize losses incurred in serving rural or small users of the service with profits earned from more lucrative market opportunities, so as to ensure that the largest number of consumers enjoy access to the system at a reasonable price.9

These traditional public policy objectives have been sharply eroded for transportation companies by deregulation. Let us explore

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5 See e.g.,MacAvoy & Robinson, Winning By Losing, 1 YALE J. REG. 1 (1983).

6 See Basedow,Common Carriers--Continuity and Disintegration in United States Transportation Law, 13 TRANSP. L.J. 1, 3-14 (1983).

7 See Dempsey, Rate Regulation and Antitrust Immunity in Transportation, 32 AM. U. L. REV. 335, 345-49 (1983) [hereinafter cited as Rate Regulation]; W. JONES, REGULATED INDUSTRIES (2d ed. 1975).

8 See generally, A. KAHN, 2 THE ECONOMICS OF REGULATION 220-46 (1971).

9 See MacAvoy & Robinson, Losing By Judicial Policymaking: The First Year of the AT&T Divestiture, 2 YALE J. REG. 225 (1985).

the impact of this erosion upon a cluster of interests regulation was created to protect.

II. ORIGINS OF ECONOMIC REGULATION

The legislative history of economic regulation is replete with public policy concerns over access by small and rural communities to the common carrier system. Federal economic regulation of American industry began, in earnest, in 1887 with the creation of the nation's first independent regulatory agency, the Interstate Commerce Commission. Transportation was the first American industry to be regulated and, paradoxically, the first to be significantly deregulated.

In an early point in our history, it was recognized that the economic development of the interior of the North American continent required that a transportation infrastructure be built. Railroads were encouraged to lay track to the west with the economic incentives of generous federal and state land grants, loans, bonds, purchases of stock, and remission of taxes.10 But not long after the tracks were laid, farmers began to object to the excessively high rates being charged them by the monopoly railroads for grain movements to eastern markets.11

It was, in large part, a pre-Populist agrarian political movement that brought about economic regulation. The Grangers succeeded first in securing legislation in several states requiring railroads to charge "just and reasonable" rates, and prohibiting rate and service

10 P. DEMPSEY & W. THOMS, LAW & ECONOMIC REGULATION IN TRANSPORTATION 7 (1986) [hereinafter cited as P. DEMPSEY & W. THOMS].

11 Id. at 8-9. See D. BOWERSOX, P. CALABRO & G. WAGENHEIM, INTRODUCTION TO TRANSPORTATION 164 (1981).

discrimination. The U.S. Supreme Court had no difficulty sustaining the lawfulness of economic regulation in its seminal decision of Munn v. Illinois[12]:

> [I]t has been customary in England from time immemorial, and in this country from its first colonization, to regulate ferries, [and] common carriers . . . and in so doing fix a maximum charge to be made for the services rendered . . . .
> [W]hen private property is "affected with a public interest, it ceases to be juris privati only." . . . Property does become clothed with a public interest when used in a manner to make it of public consequence, and affect the community at large. . . .
> [Common carriers stand] in the very "gateway of commerce," and, take a toll from all who pass. Their business most certainly "tends to a common charge, and is becoming a thing of public interest and use."[13]

Congress filled the void in interstate regulation in 1887 with the Act to Regulate Commerce. The statute established the ICC, and gave it jurisdiction to ensure that rail rates were both nondiscriminatory, and just and reasonable. Hence, the protection of small shippers and small communities from the extraction of exorbitant profits by the railroads was a major purpose of the legislation. It was also, in part, a response to the abuses of laissez faire, and the excessive concentrations of wealth and power that had resulted from it.

Market failure again became the catalyst for economic regulation during the Great Depression. Excessive capacity engendered by economic collapse and unlimited entry depressed freight rates and caused thousands of motor carrier bankruptcies during the 1930s. Our

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12 94 U.S. (4 Otto) 113 (1877).

13 Id.

elected representatives feared that a continuation of that trend might lead to a deterioration of service and higher prices for small shippers and rural communities, while the surviving carriers concentrated on high-revenue traffic lanes.14 Therefore, Congress expanded the Commission's authority over surface transportation by adding bus and trucking companies to the ICC's jurisdiction with the promulgation of the Motor Carrier Act of 1935.

In 1938, Congress added airlines to the regulatory scheme, creating another transportation regulatory agency, the Civil Aeronautics Board. One of the major proponents of the legislation, Colonel Edgar Gorrell, noted that, "In spreading out into the regions of light-density traffic and developing smaller communities, the small lines have performed an incalculable service to the country. It must be assured, through certificates, that they may continue to perform such a service, and they must be given an opportunity to protect themselves against even the possibility of oppressive competition."15 Hence, entry regulation was imposed upon the infant airline industry, in part, so that small communities would have access to this emerging mode of transport.

In 1940, Congress promulgated the first "National Transportation Policy". Among its principal objectives was "the establishment and maintenance of reasonable charges for transportation services, without unjust discriminations, [or] undue preferences or advantages . . . all to the end of developing, coordinating, and preserving a national transportation system . . . adequate to meet the needs of the commerce

14 Rate Regulation, supra at 344.

15 Quoted in Rise and Fall of the CAB, supra at 108.

of the United States . . . ."16 This cumulative body of legislation reflects a strong Congressional policy that the public in rural areas be protected against pricing and service discrimination.

III. DEREGULATION LEGISLATION AND ITS IMPACT UPON SMALL TOWNS AND RURAL COMMUNITIES: TALES FROM THE DARK SIDE

In 1979, before the full impact of air and bus deregulation had been felt, and prior to the contemporary farm crisis,17 Sen. Roger Jepsen painted a rather drab portrait of rural America:

> Approximately 34 percent of the U.S. population--some 85 million people--and 52 percent of the Nation's poor, live outside metropolitan areas.
>
> Many of these rural residents--especially the rural poor, elderly, handicapped, and young--are isolated and immobile, and face extreme difficulties in gaining access to jobs, health care, social services, shopping, recreation and friends. .. .
>
> Fifteen percent of rural households, 57 percent of the rural poor, and 45 percent of the rural elderly do not own an automobile; . . .
>
> Only 31 percent of the Nation's 20,000 towns with a population of 50,000 or less are served by a public transit system; . . .
>
> Intercity bus lines serve only about half of the Nation's towns of 50,000 or less; . . .
>
> An estimated 60 percent of places less than 2,500 population have no taxi service; and
>
> Rural residents must travel farther than their urban counterparts to gain access to medical care and essential social services--for example, 20 percent of rural residents as

16 49 U.S.C. preceding sec. 1 (1975); 49 U.S.C. sec. 10101 (1986). A similar policy was subsequently promulgated for air transport. 49 U.S.C. sec. 1302 (1975).

17 Today, America's agricultural heartland is undergoing the worst economic crisis in half a century, with 2,000 family farms going "belly up" every week. See Walljasper, Little Cell On the Prairie, THE NATION (Oct. 25, 1986), at 402. Almost 30% of the nation's farms are on the road to bankruptcy. Bitter Harvest, NEWSWEEK (Feb. 18, 1985), at 52.

> compared to 10 percent of urban residents, must travel more than half an hour to medical care.18

However bleak things may have looked when Senator Jepsen spoke these words in 1979, they were to grow progressively worse during the ensuing years.

Legislation giving carriers flexibility to abandon service to small communities has come in three major waves. The Interstate Commerce Commission was vested with the power to reverse state PUC denials of rail passenger discontinuances in 1958; by 1970, the ICC was virtually taken out of the business altogether, with the creation of Amtrak. Similarly, with the promulgation of the Airline Deregulation Act of 1978, and the sunset of the Civil Aeronautics Board on December 31, 1984, there is hardly anything left of domestic airline economic regulation.19 Under its provisions, state jurisdiction over intrastate air service is totally preempted. And, the Bus Regulatory Reform Act of 1982 gave the ICC jurisdiction to reverse PUC denials of bus discontinuances and rate increases. Let us examine each of these statutes in greater detail, and the impact each has had upon small towns and rural communities.

A. The Transportation Act of 1958

In 1929, some 20,000 passenger trains provided daily intercity service in the United States.20 Almost every town and village in the

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18 Oversight On Rural Transportation, Hearings Before the Subcomm. On Rural Development of the Senate Comm. on Agriculture, Nutrition, and Forestry, 96th Cong., 1st Sess. 26-27 (1980).

19 For a review of airline regulation in foreign commerce, see P. DEMPSEY, LAW & FOREIGN POLICY IN INTERNATIONAL AVIATION (1987).

20 W. THOMS, REPRIEVE FOR THE IRON HORSE 12 (1973) [hereinafter cited as W. THOMS].

nation enjoyed rail passenger service. But after World War II, railroads found passenger service increasingly unprofitable, and wanted out. Under section 1(18) of the Interstate Commerce Act, they could apply to the ICC for a certificate of "public convenience and necessity" to abandon the entire line.21 Under the statute, the ICC must consider whether the abandonment "will have a serious, adverse impact on rural and community development."22 The impact of a rail abandonment upon a community was, and is, devastating, for when the line is gone, it is usually gone forever. Many of the ghost towns of the West owe their demise to the decision of the railroads to terminate service.23 And since promulgation of the Staggers Rail Act of 1980, rail lines have been disappearing from rural areas at an accelerated rate, leading to drastic increases in transportation costs.24

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21 Dempsey, Entry Control Under the Interstate Commerce Act: A Comparative Analysis of the Statutory Criteria Governing Entry in Transportation, 13 WAKE FOREST L. REV. 729, 734 (1977).

22 49 U.S.C. sec. 10903(a).

23 See e.g., Abandonment of Branch Line By Colo. & So. Ry., 72 I.C.C. 315 (1922).

24 See Thoms, Clear Track for Deregulation -- American Railroads, 1970-1980, 12 TRANSP. L. J. 183, 187 (1982) [hereinafter cited as Clear Track for Deregulation]. ICC policies on rail abandonments have become dramatically more permissive since 1979, so that the number of denials in the 1980s have been reduced to an insignificant portion of cases decided. T. KEELER, RAILROADS, FREIGHT AND PUBLIC POLICY 105 (1983). For a criticism of the ICC's lax approach, see Georgia Public Service Commission v. United States, 704 F.2d 538 (5th Cir. 1983). Since the Staggers Act was passed, the ICC has granted 1,298 abandonment applications and denied 26. Appendix to Letter from ICC Office of Transportation Analysis Director Leland Gardner to Paul S. Dempsey (Mar. 16, 1987). This is a grant rate of more than 98%.

"Almost 5,000 miles of rail lines are closed each year . . . . The small towns that dot America's farm belt are being abandoned by railroad companies . . . ." Dorgan, Disappearing Railroad Blues, THE PROGRESSIVE (Aug. 1984), at 32. Shippers which have lost rail service, but have been able to secure alternative transportation, have

But to rail companies, the wholesale abandonment of particular lines was often not an attractive alternative during the 1950s, because freight service operating over them was frequently profitable. Passenger demand for rail service began to decline after World War II, principally because of a loss of traffic to the competing modes (i.e., airplanes, buses, and automobiles). Trucking competition for freight also intensified, making the cross-subsidy more difficult to maintain. Hence, railroads filed applications with the state regulatory commissions requesting permission to discontinue specific passenger trains. These applications would sometimes be denied by the state PUCs, on grounds that the railroad's overall operations, its intrastate operations, and/or its combined freight and passenger operations over the involved line were profitable, and the public's need for the service outweighed the carrier's economic losses in providing it. The PUCs viewed railroads as common carriers with a duty to provide a reasonable level of service to the communities through which they passed.

The railroads sought legislative relief from the economic burden of using freight profits to cross-subsidize passenger losses. Congress responded with the Transportation Act of 1958, which added section 13a to the Interstate Commerce Act.25 The statute allows the Interstate Commerce Commission to reverse PUC denials of rail discontinuance applications if the ICC concludes that such action is

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suffered an average 83% increase in transport costs. Ernst & Whinney, Shipper Responses To Rail Service Loss: An Assessment of Case Studies 1 (1981).

25 See Peterson, An Economic Analysis of Statutory Changes in Rail Carrier Entry and Exit, 13 TRANSP. L.J. 189, 210-13 (1984).

warranted by the public convenience and necessity, and that a continuation of the service would "constitute an unreasonable burden on the interstate operations of the carrier or on interstate commerce."26

The first opportunity for the U.S. Supreme Court to review the application of these statutory provisions involved an ICC reversal of a decision of the North Carolina Utilities Commission to disapprove the Southern Railway's proposal to discontinue the last pair of trains between Greensboro and Goldsboro, N.C.27 Between 1951 and 1956, the state Commission had approved 42 of the 44 rail discontinuance proposals that had been filed. Although rail passenger demand had declined over the line, and the cost of providing passenger service was three times its revenue, the North Carolina Commission found that the Southern Railway was a healthy carrier, that its combined freight and passenger operations over this line were profitable, and that it had done little to market its passenger service. Although the state Commission had approved the Southern's prior proposals to discontinue two other pairs of trains, it found a strong public interest in retaining the last pair serving the market. But the Supreme Court sided with the ICC, finding that where the public demand for service in not great, the ICC need give little or no weight to the carrier's overall prosperity in reversing a state's denial of a rail discontinuance application.28

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26 49 U.S.C. sec. 10909.

27 Southern Ry. Co. v. North Carolina, 376 U.S. 93 (1964).

28 Id.

With this expansive interpretation given the new statute by the U.S. Supreme Court, rail discontinuances of passenger service became robust. Less concerned with the impact of the loss of service upon local populations, the ICC was significantly more liberal in granting rail discontinuance proposals than the states had ever been.29 Under ICC review, the number of passenger trains fell by 60% between 1958 and 1970.30 By 1970, only 360 intercity trains were left.31

Congressional concern over the rapidly shrinking intercity rail network led it to promulgate the Rail Passenger Services Act of 1970, which allowed railroads to terminate their passenger operations by turning them over to a newly formed federally-subsidized corporation, Amtrak.32 Amtrak began operation on May 1, 1971, with 225 trains. During the conversion from private to Amtrak service, another 500 communities lost intercity passenger train service.33

In recent years, efforts to diminish government's role in the market have been expanded to embrace not only economic deregulation, but also elimination of federal subsidies in transportation. Since the beginning of the Reagan administration, every White House budget proposal has moved to constrict or eliminate Amtrak's funding. A significant reduction in federal subsidies to Amtrak would force it to

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29 Clear Track for Deregulation, supra at 197.

30 Id. at 191; P. DEMPSEY & W. THOMS, supra at 73.

31 W. THOMS, supra at 12.

32 Id. See Johnson, Lessons From Amtrak and Conrail, 49 ICC PRAC. J. 247, 250-51 (1982).

33 Letter from W. Graham Claytor, Jr., to Paul Stephen Dempsey (Mar. 3, 1987) [hereinafter cited as Claytor Letter].

terminate service over all of its routes except, perhaps, the Boston-Washington run.34

Amtrak today serves more than 500 communities in the United States. That is more cities than are served by all the airlines combined. Of the communities served by Amtrak, 119 have no scheduled airline service;35 upon termination of the present small community air subsidy program in 1988, that figure will likely jump to 161.36 Another 96 Amtrak-served communities have no scheduled intercity bus service; 40 have neither air nor bus service.37 Also, among Amtrak's riders are a disproportionate number of low-income and elderly travelers who cannot or will not take an alternative form of transportation.38

Today, with the skeletal intercity system that Amtrak provides, the United States compares poorly with the rest of the civilized world in terms of rail passenger service. Professor William Thoms has observed, "With the exception of the heavily-traveled Boston-

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34 Reagan Puts the Brakes On Amtrak, BUS. WEEK (Mar. 30, 1981), at 83.

35 Amtrak Reauthorization, Hearings Before the Subcomm. on Surface Transportation of the Senate Comm. on Commerce, Science and Transportation, 99th Cong., 1st Sess. 74 (statement of W. Graham Claytor, Jr.).

36 Claytor Letter, supra. The airline figure is based on availability of such service within a 30-mile radius of city center for communities east of the Mississippi, and a 50-mile radius west of the Mississippi. Id.

37 Id.

38 Amtrak's Struggle to Stay on Track, NEWSWEEK (June 3, 1986), at 50.

Washington corridor, service levels on American passenger trains are the worst in the world."39

Hence, deregulation of rail passenger service has enabled railroads to shed themselves of a money-losing operation, a relatively small portion of which has been replaced by taxpayer subsidies, while thousands of small communities have been pruned from the system. Let us examine the similar experiences of air and bus carriers.

B. The Airline Deregulation Act of 1978

Senator Jim Sasser recently pointed out the important role that the transportation infrastructure has played in supporting economic development in America:

> [I]n the 19th century . . . if you lived in an area of water or river transportation, you flourished. Along came the railroad and it appeared to have the power of economic life or death over cities . . . .
>
> Now, a strong case can be made that air service has the same impact on economic development of a region that river traffic or rail access had in an earlier era.40

The airline industry was the second major passenger transportation industry to be deregulated, with the promulgation of the Airline Deregulation Act of 1978 [ADA]. In that bill, airline exit requirements were significantly liberalized. All but the last carrier in a market is free to leave at will. Congress recognized that such policies might have a deleterious effect upon the provision of service to small communities, and therefore added section 419 to

39 Clear Track for Deregulation, supra at 196.

40 The Economic Impact of Federal Airline Transportation Policies On East Tennessee, Hearings Before the Sen. Comm. on the Budget, 99th Cong., 1st Sess. 19 (1985) [hereinafter cited as Economic Impact of Federal Airline Policies].

the Federal Aviation Act, which provides a 10 year program of federal subsidies for air service to small communities.41 The ADA's policy statement specifies that it is the purpose of the new legislation, inter alia, to maintain "a comprehensive and convenient system of continuous scheduled airline service for small communities and isolated areas, with direct Federal assistance where appropriate."42

Prior to the promulgation of section 419, many proponents of deregulation had discounted the likelihood that it would lead to any significant service reductions for small communities. A Senate subcommittee chaired by Edward Kennedy reviewed 327 "losing" city pairs served by United Air Lines; the U.S. Department of Transportation examined 160 "losing" pairs served by Eastern Air Lines. Both found that only about two dozen of the markets were served on a mandatory basis, and that in most of these, more service was provided than required by the CAB. It was predicted that in the remaining markets, if the trunk carrier pulled out, a commuter or local service carrier would fill the void, in most cases without a subsidy.43 Thus, it was alleged that small communities had little to fear from deregulation.

But there was good reason to fear a reduction in service. Even though the CAB had jurisdiction prior to deregulation to prohibit

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41 49 U.S.C.A. sec. 1389 (Supp. 1987). See Comment, Commuter Airlines and the Airline Deregulation Act of 1978, 45 J. AIR L. & COM. 685, 692-98 (1980), and Dempsey, Erosion of the Regulatory Process in Transportation, 47 ICC PRAC. J. 303, 310 (1980) [hereinafter cited as Erosion of Regulation].

42 49 U.S.C. sec. 1302(a)(8).

43 E. BAILEY, D. GRAHAM & D. KAPLAN, DEREGULATING THE AIRLINES 112 (1985) [hereinafter cited as E. BAILEY et al].

]service abandonments it deemed inconsistent with the public interest, between 1960 and 1978 it had approved the abandonment of 173 communities (or an average of 9.6 per year).44

Under deregulation, the trend sharply accelerated. In the first year of deregulation, 260 cities suffered a deterioration in air service, a disproportionate number of them being small towns.45 Seventy of the communities which were receiving some service lost all of it.46 By the second year, more than 100 communities had lost all their scheduled service.47 So, while abandonments averaged 9.6 per year before deregulation, they soared to more than 50 per year during deregulation's first two years.

More recent statistics are nearly as grim. The U.S. General Accounting Office noted that "[b]etween October 1978 and October 1984, the scheduled air service network shrank from 632 cities to 541, as the number of nonhub communities with scheduled air service decreased by 91 (23 communities gained service during the period while 114 lost service)."48 Professors Stephenson and Beier note that "there is evidence that deregulation has accelerated the withdrawal from smaller communities and that there has been a concomitant reduction in the

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44 CIVIL AERONAUTICS BOARD, COMPETITION AND THE AIRLINES 135 (1982).

45 See CIVIL AERONAUTICS BOARD, REPORT ON AIRLINE SERVICE 43-50 (1979).

46 Meyer, Section 419 of the Airline Deregulation Act: What Has Been the Effect On Air Service to Small Communities?, 47 J. AIR L. & COM. 151, 181 (1981) [hereinafter cited as Meyer].

47 Havens & Hemsfeld, Small Community Air Service Under the Airline Deregulation Act of 1978, 46 J. AIR L. & COM. 641, 673 (1981).

48 GAO REPORT, supra at 29.

frequency of direct flights in those markets."49 This is indeed a surprising consequence of deregulation, since the Airline Deregulation Act of 1978 provided for a 10 year program of federal subsidies designed to preserve essential air service to small communities. Let us take a closer look at precisely what types of service losses have been endured under deregulation.

Proponents of deregulation, when assessing its impact upon small communities, tend to emphasize the increased number of departures many have enjoyed.50 Since 1978, 410 markets have been abandoned by larger airlines flying jet aircraft.51 Many had service restored by commuter airlines, flying smaller aircraft, sometimes landing more frequently.52 But while departures may have increased for some small communities, there appears to have been a significant reduction in the number of available seats.53 By 1984, 225 airports had suffered more than a 50% decline in available seats, including some 119 airports that lost service completely.54 Moreover, a number of rural states have experienced a reduction in departures as well as seats since deregulation began.55

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49 Stephenson & Beier, The Effects of Airline Deregulation on Air Service to Small Communities, 20 TRANSP. J. 54, 57 (1981).

50 E. BAILEY et al, supra at 123; R. NOLL & B. OWEN, THE POLITICAL ECONOMY OF DEREGULATION 59 (1983).

51 See GAO REPORT, supra at 19.

52 Rise and Fall of the CAB, supra at 178, n.428.

53 Ott, Upper Midwest Mulls Service Options, AV. WEEK & SPACE TECH. (July 12, 1982), at 35, 36 [hereinafter cited as Ott].

54 M. BRENNER, J. LEET & E. SCHOTT, AIRLINE DEREGULATION 98 (1985) [hereinafter cited as M. BRENNER et al].

55 See id. at 36, and GENERAL ACCOUNTING OFFICE, DEREGULATION 34 (1985) [hereinafter cited as GAO REPORT].

Many passengers complain that the smaller unpressurized aircraft flown by commuter and local service carriers are less comfortable than the jets they replaced.56 They are certainly less safe. Depending upon how it is measured, commuter airlines have a safety record of between 3 and 37 times worse than established airlines flying jet aircraft.57

Passengers also appear to be less satisfied with service schedules and waiting times.58 With larger carriers concentrating on hub and spoke operations, small communities lost their direct flights to most large cities.59 In the first two years of deregulation, 63% of small communities having certificated service experienced reductions in nonstop service.60 Hence, air travel has become a more

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56 Oster, Jr. & Zorn, Deregulation and Commuter Airline Safety, 49 J. AIR L. & COM. 315, 316 (1984).

57 See Oster, Jr. & Zorn, Airline Deregulation, Commuter Safety, and Regional Air Transportation, 14 GROWTH AND CHANGE 3, 7 (1983), and Meyer, supra at 631, n. 222. The National Transportation Safety Board has concluded that the commuter airlines accident rate of 1.48 fatalities per 100 million passenger miles is 37 times worse than scheduled airlines. The Puddle-Jump Problem, NEWSWEEK (Oct 23, 1978), at 76 [hereinafter cited as Puddle-Jump Problem]. The GAO has found that the accident rate for commuters to be seven times higher than the rate for the large scheduled airlines, and the rate for air taxis to be 18 times higher. FAA Passenger Regulation of 9-Seat and Under Passenger Aircraft, Hearings Before the Subcomm. on Investigations and Oversight of the House Comm. on Public Works and Transportation, 98th Cong., 1st Sess. 3 (1985) (testimony of Oliver W. Krueger). See Congress Wrestles With Air Safety Concerns, 43 CONG. Q. 2293 (Nov. 9, 1985).

58 See Ahmed, Air Transportation to Small Communities: Passenger Characteristics and Perceptions of Service Attributes, 38 TRANSP. Q. 15, 21 (1984).

59 See Warren, Changing Air Transportation Services for Smaller Metropolitan Regions, 38 TRANSP. Q. 245, 265 (1984).

60 Stephenson & Beier, supra at 56-57.

circuitous adventure for many passengers.61 Assessing the quantitative and qualitative impacts, it has been noted that "smaller communities are receiving markedly worse air service than existed prior to deregulation."62 Clearly the comfort, convenience, and level of safety of air service for small communities has deteriorated.63

Even Thomas Gale Moore, a nationally recognized proponent of deregulation, admits that 40% of small communities have suffered a loss of air service since deregulation began, while ticket prices have increased disproportionately for passengers traveling to or from small communities.64 Many sources agree with this assessment. The Congressional Research Service found that fares in smaller markets are now substantially higher than those offered prior to deregulation.65 Professor Addus adds that "As a result of airline deregulation . . . fares for traveling between small points have increased rapidly; and commuter air carrier fares are reported to be particularly high in most cases."66

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61 Flying the Deregulated Skies, AV. WEEK & SPACE TECH. (July 5, 1982), at 9.

62 Meyer, supra at 182. See also, S. TOLCHIN & M. TOLCHIN, DISMANTLING AMERICA: THE RUSH TO DEREGULATE 245-46 (1983) [hereinafter cited as S. TOLCHIN & M. TOLCHIN].

63 Erosion of Regulation, supra at 304-06.

64 Moore, U.S. Airline Deregulation: Its Effects On Passengers, Capital, and Labor, 24 J. L. & ECON. 1, 15, 18, 28 (1986).

65 Quoted in Economic Impact of Federal Airline Policies, supra at 5 (testimony of Sen. Jim Sasser). The U.S. General Accounting Office also found that "passengers in many lightly traveled, short-distance city pairs did not benefit from lower fares." GAO REPORT, supra at v, 51-52.

66 Addus, Subsidizing Air Service to Small Communities, 39 TRANSP. Q. 537, 548 (1985).

These results appear to be consistent around the nation. After deregulation, passenger fares in California rose between 38% and 103%, as service to small communities deteriorated.67 The Upper Midwest Council concluded that passenger fares at smaller hubs in the midwestern states rose between two and four times the rate of fare increases at larger hubs.68 In the Dakotas, the Carolinas, Mississippi, New Mexico, Rhode Island, Tennessee, and West Virginia, the results were the same; a parade of witnesses before several Congressional Committees provided example after example of the discriminatory fares and deteriorating service resulting from deregulation.69

Prior to deregulation, air fares had been set below marginal costs in short-haul markets, and above cost in longer haul markets. For example, under the CAB's 1969 mileage-based formula, passengers flying 100 miles paid 70% of cost, while passengers flying 1,300 miles

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67 R. Brozoski, Airline Deregulation in California (California PUC, Transportation Division, Oct. 1981); O'Lone, PUC Statement Contested By Airlines, AV. WEEK & SPACE TECH. (Jan. 28, 1980), at 37. The California result is particularly interesting in light of the fact that its intrastate experience prior to deregulation was pointed to as a model of the benefits which could be accomplished by deregulation. See Note, Is Regulation Necessary? California Air Transportation and National Regulatory Policy, 74 YALE L.J. 1416 (1965); Edles, The Strategy of Regulatory Change, 49 ICC PRAC. J. 626, 628 (1982).

68 Ott, supra at 36.

69 See Economic Impact of Federal Airline Policies, supra. The Economic Impact of Federal Airline Transportation Policies On East Tennessee, Hearings Before the Senate Comm. on the Budget, 99th Cong., 1st Sess. (1985). Field Hearing On Aviation Matters, Hearings Before a Subcomm. of the Senate Comm. on Appropriations, 98th Cong., 2d Sess. (1984). See also, Impact of Airline Deregulation On Service To Small and Medium Sized Communities, Hearings Before the Subcomm. on Aviation of the Senate Comm. on Commerce, Science, and Transportation, 96th Cong., 1st Sess. (1979).

paid 109% of cost.70 The airlines were forced to cross-subsidize losses incurred in serving small communities with profits earned in serving larger markets.71

The real impact of airline deregulation, however, will not be felt until 1988, when federal subsidies for service to small communities expire.72 Nearly 150 communities today receive subsidized service under the section 419 program.73 Most will lose air service altogether when federal subsidies dry up, next year.

The loss of service will ripple perniciously throughout the economy of each of these communities. A survey of the top 500 firms in America reveals that 80% of them will not locate their facilities in an area which does not have easily accessible air transportation.74 By increasing transportation costs and decreasing accessibility, deregulation is having a deleterious effect upon the ability of small communities to attract new investments (or indeed, to keep existing

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70 GAO REPORT, supra at 22.

71 "The historical cross-subsidy polity resulted in some communities getting air service they otherwise would not have. The fare formula benefited passengers in short-distance or lightly traveled markets because they generally paid fares below the cost of the service they received." Id. at 23.

72 See M. BRENNER et al, supra at 102.

73 See GAO REPORT, supra at 31-32.

74 Economic Impact of Federal Airline Policies, supra at 12-13 (testimony of Eugene Joyce).

businesses from leaving).75 Similar conclusions reached by the Southern Growth Policies Board have been summarized as follows:

> [There is an important trend] in economic development . . . toward greater growth in the nonmanufacturing or service sector, especially in the higher-technology industries. These firms rely . . . heavily on recent technological advances in communications and information systems, and good air service has become an essential ingredient in their location decisions. Air service is as important to these firms as electricity and telephone communications; and in this sense, air service should be considered a public utility 76

Susan and Mark Tolchin, in their comprehensive assessment of the impact of deregulation, reached similar conclusions, addressing the external costs of service deterioration:

> The real problem with economic deregulation is that the transportation system, the airwaves, and the banks are national resources, affecting many segments of the population with no immediate connection to the affected industries. A bankrupt airline can leave a city without adequate air transportation, damaging that city's ability to compete in the business community and reducing the quality of life for its residents. In that sense, the traditional lines between economic and social deregulation become blurred. A bankrupt airline, the development of a ghost town, and the closing of a company represent upheavals with such enormous impact that some

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75 Meyer, supra at 175. See Puddle-Jump Problem, supra; and When the Jets Stopped Flying at Bakersfield, BUS. WEEK (Nov. 5, 1979), at 106. Many observers agree. "Deregulation has brought inconveniences to many and a sense of isolation to others, touching the lives of businessmen wanting connections to the national transportation system, and of vacationers . . . . Threat of further air service losses, at least disruptions, at the scheduled conclusion of federal subsidies, has been an additional psychological blow to communities seeking to develop or even maintain current status . . . ." Ott, supra at 36.

76 Economic Impact of Federal Airline Policies, supra at 16-17 (testimony of William Willis).

> measure of public protection is more than justified. And who else but a public agency can serve as the ultimate arbiter, stabilizing the kind of erratic market conditions that brought about the creation of these agencies in the first place?77

C. The Bus Regulatory Reform Act of 1982

With the passenger trains having vanished from rural America, and with commercial aircraft no longer landing at many small town airports, the only means of public intercity transport left was the bus.

Prior to its deregulation, industry officials quite candidly predicted that deregulation would result in a drastic reduction in service to small communities. Harry Lesko, President of Greyhound, said that "Eighty-nine percent of our routes are subsidized by the bread-and-butter primary routes . . . . [I]f we are to keep our lines running and the scheduled miles operating on the primary routes to satisfy the high-density population factors, the rural areas are going to have to suffer because they're straining the main line system."78 Similarly, Charles Webb, President of the National Association of Motor Bus Owners, argued that "[t]he one conclusive argument against removal of controls on entry by motor carriers of passengers stems from their obligation to provide service to thousands of small cities and towns and to vast rural areas without profit or at a loss, and from the fact that it would be unconscionable either to permit new entrants to skim the cream of traffic or to authorize existing

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77 S. TOLCHIN & M. TOLCHIN, supra at 250.

78 Intercity Bus Service In Small Communities, Senate Comm. on Commerce, Science and Transportation, 95th Cong., 2d Sess. 17 (1978).

carriers to discontinue bus service to thousands of communities having no other form of public transportation."79 Nevertheless, as with allegations of cross-subsidy made by the airlines prior to deregulation, these too were discounted by Congressional committees considering deregulation.80

The Bus Regulatory Reform Act of 1982 gave bus companies significant new freedom to abandon or discontinue service, and to raise fares. These provisions follow the pattern for railroads established by section 13a, discussed above, allowing the ICC to reverse state PUC denials, and thereby largely preempting State jurisdiction over the question.81 Note that while bus companies are

79 Webb, Legislative and Regulatory History of Entry Controls on Motor Carriers of Passengers, 8 TRANSP. L.J. 91, 105 (1976).

80 Id.

81 See Kahn, The Bus Regulatory Reform Act of 1982 and Federal Preemption of Intrastate Regulation of the Intercity Bus Industry: Where Has It Come From? Where Will It Lead?, 14 TRANSP. L.J. 179 (1986) [hereinafter cited as Kahn]. Where a State has either denied a discontinuance request, or failed to act within 120 days, the bus company may seek reversal by the Interstate Commerce Commission. For existing operating authority, the ICC must approve the discontinuance unless it finds that it would be inconsistent with the public interest, and that continuing the service will not constitute an unreasonable burden on interstate commerce. The ICC must also give great weight to the extent to which the carrier's combined interstate and intrastate operations generate revenues less than the variable costs of providing service on the route. 49 U.S.C. sec. 10935. It must also consider the national transportation policy, whether the carrier has received a subsidy offer, and whether the service is the last bus service in the area and, if so, whether reasonable transportation alternatives exist. Id. However the fact that a community would be left without bus service is not, in and of itself, sufficient grounds for denying the discontinuance request. See Katzman, The Bus Regulatory Reform Act of 1982: What It Does and How It Works, 52 TRANSP. PRAC. J. 221, 238-43 (1985).

The ICC is also granted appellate review over state ratemaking determinations by the 1982 Bus Act. On appeal, the ICC may reverse a state denial of a rate increase if it finds that the intrastate rate discriminates unreasonably against, or imposes an unreasonable burden on, interstate commerce. There is a rebuttable presumption that the intrastate rate is unreasonable if it is lower than either the

free to appeal state denials of discontinuance applications or proposed rate increases to the ICC, the public enjoys no corresponding right of appeal when the state grants the discontinuance or rate increase.

The ICC has taken an extremely liberal approach to deregulation here as well.82 It has placed the burden of proving that a bus discontinuance will not impose an unreasonable burden on interstate commerce upon protestants, those least likely to have access to the relevant information to prove it.83 In reversing the Oklahoma Corporation Commission's denial of a bus discontinuance application (on grounds that many communities would be left without alternative means of public transport), the ICC held that "the policy of the Bus Act . . . favors exit from unprofitable routes and the reduction or elimination of cross-subsidies wherever possible."84 As a Commissioner of the N.Y. Department of Transportation noted, "In case after case . . . the ICC has shown a total disregard and lack of concern for the welfare of the riding public."85

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comparable interstate rate or the variable costs of providing the service. 49 U.S.C. sec. 11501(e)(2).

82 See Kahn, supra.

83 Department of Transportation and Related Agencies Appropriations for Fiscal Year 1985, Hearings Before a Subcomm. of the Senate Comm. on Appropriations, 98th Cong., 2d Sess. 476-77 (1985) [hereinafter cited as Appropriations Hearings].

84 Missouri, Kansas and Oklahoma Coach Lines--Oklahoma Corp. Comm'n, No. MC-C-36364 (ICC served Feb. 29, 1984).

85 Household Goods Transportation and Bus Regulatory Reform Oversight, Hearings Before the Subcomm. on Surface Transportation of the Senate Comm. on Commerce, Science and Technology, 99th Cong., 1st Sess. 145 (statement of John D. Mladinov) [hereinafter cited as Bus Oversight]. A prominent Washington, D.C. attorney expressed similar concerns: "In practice, the ICC is utilizing an interpretation of the BRRA which leads to the granting of relief to any carrier which comes

Since promulgation of the 1982 Bus Act, carrier abandonments have been little short of breathtaking:

> An ICC survey of bus companies after only 11 months of deregulation found that 1,294 locations were reported as having been dropped or proposed to be dropped from intercity routes. That is almost 10 percent of all the communities directly served by intercity buses at the time of deregulation.
>
> Of these 1,294 locations, 776 lost all of their intercity service. The vast majority of those communities have less than 10,000 residents. In less than 1 year, almost 1 million people lost their bus service. . . . [B]etween 1975 and 1982, the number of communities receiving bus service declined at an annual rate of 3.3 percent. In the 2 years following enactment of the Bus Act, that rate has tripled; three times as many communities are losing intercity bus service now than before deregulation. Prior to deregulation, the average number of service terminations to communities was 147 per year; since deregulation, that rate has increased over 200 percent, to over 300 terminations per year.
>
> A figure that makes an even more telling statement of the effect of deregulation is the ratio of service terminations to service initiations. The proponents of deregulation claimed that reducing entry barriers as well as exit barriers would be in the public interest. While it does not appear to have worked out that way, the DOT study found that before deregulation service terminations outnumbered service initiations almost 4 to 1. Since 1982, however, that figure has more than doubled. Specifically, for every community that receives new service, 8.6 communities lose their service.86

Hence, in less than a year after deregulation, more than a thousand communities in 40 states lost all their bus service.87 In

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before it, provided there is at least a tenuous link with interstate commerce." Kahn, supra at 198-99.

86 Bus Oversight, supra at 2 (testimony of Sen. Larry Pressler).

87 Shane, Opinion From the Executive Office, TRAVEL-HOLIDAY (Mar. 1984), at 61.

1983, Greyhound alone proposed to eliminate 4,300 miles of service to more than 1,300 stops in 43 states.88 Greyhound and Trailways (which together dominate 80% of the regular route passenger market) used their new freedom to boost intrastate fares, in some cases as much as 25%.89 Today, there exists a high incidence of rate discrimination, by which passengers from small communities pay relatively higher rates than their urban counterparts.90

By late 1986, 4,514 communities had lost bus service, while only 896 had gained it. The big losers have been small communities; 3,432 of the towns which have lost service have a population of 10,000 or less.91 The vast majority now have no alternative means of intercity public transport.92 The loss of bus service not only adversely affects passengers dependent upon personal transportation, but also eliminates express small parcel service for small businesses.

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88 Now That the Brakes Are Off the Bus Industry, U.S. NEWS & WORLD REP. (Apr. 18, 1983), at 87.

89 Id. Blyskal, Leave the Driving to Adam Smith, FORBES (Aug. 1, 1983), at 100.

90 Oversight of the Household Goods Transportation Act of 1980 and the Bus Regulatory Reform Act of 1982, Hearings Before the Subcomm. on Surface Transportation of the Senate Comm. on Commerce, Science and Transportation, 98th Cong., 2d Sess. 25 (1984) (statement of David N. Gibson).

91 Letter from ICC Chairman Heather Gradison to Senator Larry Pressler (Sept. 8, 1986).

92 The ICC found in January 1984, that of 1,294 points destined to lose bus service, 1,045 had no alternative service. Appropriations Hearings, supra at 479 (testimony of Sen. Mark Andrews).

Trailways has announced plans to abandon all of Colorado, Montana, Nebraska, South Dakota, Wyoming and much of Kansas.93 One source notes that "[t]he trend toward cuts in service is continuing at a rapid pace, with dozens of communities throughout the Middle West facing possible loss of their last means of public transport."94 The Illinois Commerce Commission has concluded that "the effect of the Act on rural and small city Illinois has been severe, [with] whole areas of nonmetropolitan Illinois . . . taken from the state bus network, without compensating gains in the more populated regions."95 Senator Larry Pressler notes that "[b]us deregulation has had a devastating impact on rural America. . . . Low income families and the elderly are disproportionately affected because it is they who most heavily rely on the service."96 Professor Thoms agrees:

> Arrayed against the duopoly of the bus system are customers who are in no position to bargain at arm's length. Bus travelers are often poor people with no alternatives. Many do not own cars. Many are too young, too old, or too infirm to drive. . . . Deregulation of air and rail . . . has meant that many cities, towns and rural areas have lost scheduled service.97

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93 Dempsey, Deregulation Stranding Residents of the Lone Prairie, Rocky Mountain News, Sept. 14, 1986, at 73 [hereinafter cited as Deregulation Stranding Residents].

94 Robbins, Dependent on Buses, Midwestern Towns Fight Cuts In Service, New York Times, Oct. 14, 1986, at A14.

95 ILLINOIS BUS SERVICE SINCE THE BUS ACT: A DIMINISHING INTERCITY NETWORK (1984).

96 Id.

97 Thoms, Unleashing the Greyhounds -- The Bus Regulatory Reform Act of 1982, 6 CAMPBELL L. REV. 76, 94 (1984). See also, F. THAYER, REBUILDING AMERICA: THE CASE FOR ECONOMIC REGULATION 97-98 (1984).

IV. CONCLUSION: "YOU CAN'T GET THERE FROM HERE"

Transportation, communications and energy are the foundation upon which the rest of commerce is built. Government policies can have a powerful influence on locational decisions and economic development by virtue of the role they play in the "construction, subsidy, taxation and regulation of carriers and the means of communications."98

Trade routes are the arteries of the economic system, linking every city, town, and hamlet to the life blood of commerce.99 Transportation and economic development are mutually interdependent -- transportation improvements stimulate economic growth, and that growth, in turn, increases the demand for transportation.100 The converse is also true. The absence of reasonably priced transportation will stifle economic development and cause a region's economy to spiral downward.101 These features distinguish the infrastructure industries from most others in the economy, and explain one of the major reasons why such services have been regulated since an early point in Anglo-American history. In order for the vast rural areas of this nation to have a healthy economy, small towns must have

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98 E. HOOVER, THE LOCATION OF ECONOMIC ACTIVITY 255 (1948).

99 "Transportation has been a fundamental element in the growth of civilization and industrial development, and has had a profound effect on collective economic growth." Rate Regulation, supra at 335. Even Adam Smith recognized that the breadth of the market depends upon the price and availability of transportation. A. SMITH, THE WEALTH OF NATIONS I: 19-22 (1925).

100 Addus supra at 551-52.

101 See Erosion of Regulation, supra at 311.

non-discriminatory access to the infrastructure industries, or they will be isolated from the mainstream of commerce, and wither on the vine.

Economic regulation has traditionally protected public interest values that might not find a high priority in the marketplace. It has treated common carriers (e.g., the airlines, railroads, bus and telephone companies) as industries imbued with a unique responsibility to satisfy the needs of the public for universal service. Small communities as well as large (and small businesses as well as large) have traditionally been required to be served at a non-discriminatory price.102 While the invisible hands of the marketplace have made most of the decisions regarding the level of service and price to be provided, regulatory agencies have traditionally made a few, establishing the metes and bounds of performance, so as to protect the public interest.103

Regulation imposes upon common carriers both a burden and a benefit. The burden is the obligation to provide an adequate level of service to all geographic areas within their operating territory, at reasonable prices. Traditionally, this approach has fostered a policy for distributing wealth, whereby somewhat higher profits earned from the larger users of the system have cross-subsidized below cost pricing to relatively smaller, or more remotely located users. In return for providing this benefit to small communities, the regulated

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102 See ICC Disintegration, supra at 48.

103 See Waring, Motor Carrier Regulation -- By State Or By Market?, 51 ICC PRAC. J. 240, 242 (1984).

enterprise has been granted a franchise of operating authority which shields it from competitive entry and "cream-skimming" by rivals.

How has this changed under deregulation? Competitive entry has forced down prices for larger users, eliminated the ability of carriers to cross-subsidize, and thereby led carriers to raise prices and abandon service to small users. The President of the South Dakota Chamber of Commerce put it this way: "The federal government's deregulatory steps of the last decade governing milk prices, railroads, trucking, airlines and telephone service have resulted in higher prices and reduced service."104 Such are the demons that leapt out of Pandora's box of deregulation.105 And they were unleashed at a time when America's rural areas are reeling from the most disastrous economic environment for agriculture since the Great Depression.106 In a recent study, several economists have noted that "the convergence of rural and urban incomes seems to have stalled and the remaining gap will be more difficult to remove because of structural forces at work . . . [including the fact that] deregulation appears to have forced businesses in many rural areas to pay higher . . . transportation rates than in the 1970s . . . ."107 The combination of deregulation

104 Ott, supra at 35.

105 Deregulators used the theory of contestable markets to rebut allegations that carriers enjoying a monopoly or oligopoly presence in a market would earn supra-competitive profits there. In theory, another carrier should enter in such circumstances and restore the competitive equilibrium. Yet, the empirical data suggests that the theory has not proven true in the post-deregulation environment. Moore, supra.

106 Lewis, The US Farm Crisis: Measuring the Ripple Effect, CERES (Mar.-Apr. 1986), at 41.

107 Henry, Drabenstott & Gibson, A Changing Rural America, FEDERAL RESERVE BOARD OF KANSAS CITY ECONOMIC REVIEW 23, 38 (July/Aug. 1986). "In the past, regulation contributed to lower interest rates and

and the farm crisis will mutually ensure the degeneration of many small towns into "rural ghettos".108

In the United States, public subsidies have been offered to ameliorate the political opposition to deregulation by legislators representing rural constituencies. Yet, in the long term, we see that they become impossible to maintain by a federal government unable to balance its budget. Small community airline subsidies will expire next year. And, probably sooner rather than later, Amtrak will disappear as its subsidies are terminated. In America, these days, if the market doesn't provide it, it usually doesn't exist.109

Under deregulation, the service obligations of common carriers have become impossible to maintain. The most lucrative markets have

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transportation costs in rural areas than in metropolitan areas. Recently, though, deregulation has brought new market forces to bear on rural areas. And coming at a time when the rural economy was under many downward pressures, the effects of deregulatioan may have contributed to that stress." Id. at 39.

108 "A blight that is economical rather than botanical is transforming small towns in the Midwest into rural ghettos--pockets of poverty, unemployment and despair." See Davidson, The Rise of the Rural Ghetto, THE NATION (June 14, 1986), at 820.

109 Although section 419 and Amtrak subsidies have been addressed herein, the broader question of state taxpayer subsidies is beyond the scope of this article. But note that those that do exist in many areas of transportation (i.e., for Amtrak, urban mass transit, the U.S. Postal Service, and the section 419 small community air services program) have come under heavy political assault by a federal government struggling in the 1980s with $200 billion a year deficits. Some states do provide Amtrak subsidies. See Nice, The States and Amtrak, 40 TRANSP. Q. 559 (1986); and P. DEMPSEY & W. THOMS, supra at 286-88. But most rural states are, these days, suffering stiff budget deficits of their own, and are least able to afford transportation subsidies. Moreover, although statutory subsidy provisions exist, not only for Amtrak, but also for rail abandonment and bus discontinuance proposals, they have, in some instances, proven administratively unworkable. See Michel, Casenote: Chicago and North Western Transportation Company v. United States, 13 TRANSP. L.J. 245 (1984), and Mills, The Lake Geneva Line: A Case History, 52 TRANSP. PRAC. J. 51 (1984).

become flooded with entrants, thereby squeezing carrier profits and making exit of marginal markets inevitable.110 Today, when a passenger asks for a ticket to Bountiful, the clerk must answer, "You can't get there from here."111 And if telecommunications follows the same route, residential consumers will pay higher prices for poorer service.

And so, the trains, the jets, and the buses have disappeared from much of rural America. Ultimately, those without the private automobile will be left stranded. The economic base of isolated communities will become increasingly difficult to sustain. Without adequate transportation and communications services, many towns in America's heartland will slowly die.

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110 Transportation Deregulation, supra at 356-59, 381-82. Dempsey, Deregulation's Toll Is Rising, Denver Post, Sept. 4, 1986, at 5B.

111 See W. Thoms, You Can't Get There From Here -- Intermodal Passenger Transportation in North Dakota (Oct. 1978). O. NASH, YOU CAN'T GET THERE FROM HERE (1958).

Perspective

A forum—ideas, analysis, opinion

Chicago Tribune, Friday, October 14, 1983 Section 1 19

Stormy skies of deregulation

By Paul Stephen Dempsey

The desperation tactics of Frank Lorenzo [who gutted Continental Airlines and destroyed its unions] and Frank Borman [who threatened to do the same to Eastern] come as no surprise to anyone who has observed the transportation industry twist and turn in the icy winds of deregulation. No industry can continue to suffer the catastrophic economic losses of the last few years without comprehensive readjustment.

There is no adjective but catastrophic to describe the airline industry's economic losses since deregulation was inaugurated. In 1980, it suffered its most severe losses in the history of domestic aviation up to that time, an astonishing $280 million. The following year, the 12 largest carriers surpassed this threshold by threefold, losing $641 million. Worldwide industry losses for 1982 were an astounding $900 million. And in the first quarter of this year, the nation's airlines lost more than half a billion dollars.

Proponents of the free market have insisted that deregulation was not the cause of the industry's problems; instead, high fuel prices, the recession and poor management were the culprits. But fuel prices began to recede with the loss of OPEC's grip on the oil-glutted West. With every dollar the price of oil drops, United Airlines alone saves a hefty $1.8 billion. And the recession ended this year.

In addition to Braniff, bankruptcies have already ravaged Air New England, El Al, Laker and now Continental, not to mention a host of smaller carriers. Among those remaining, many find themselves on the endangered species list, including Air Florida, Eastern, Pan Am, Republic and World. Never have so many suffered so severely in such a short period of time.

The bankruptcy and reorganization of Lorenzo's Continental constitute merely a forerunner of the survival tactics likely to be employed by many other carriers in the next several years.

United and American Airlines, the nation's two largest, were the only major carriers to have supported deregulation when it was first promoted by the Carter administration in the late 1970s. Curiously, American airlines profits most from Braniff's demise [for they both share the Dallas hub], and United celebrates a retrenched Continental [they share the Denver hub with Frontier]. Both United and American performed well in the second quarter of this year. In contrast, during the second quarter a number of their competitors suffered enormous losses: Eastern [$12 million], Continental [$14 million], TWA [$16 million], Republic [$44 million] and even traditionally strong Delta [$51 million].

Larger, deep-pocketed competitors can undoubtedly survive the vicissitudes of the market cycle and the cut-throat fare wars precipitated by deregulation. But if more and more medium size carriers fail, the airline industry may well come to resemble the deregulated rail industry, which is today dominated by only seven railroads [soon to be reduced to a half dozen with the forthcoming Santa Fe-Southern Pacific merger]. After the shakeout, in those markets in which the surviving air carriers enjoy a monopoly or oligopoly, super saver, promotional and excursion fares will vanish.

Hence, the short term benefits of pricing competition may eventually be overshadowed by long-term consequences of deregulation. The motor carrier industry is experiencing the same phenomenon—almost 300 truck lines have gone "belly up" since deregulation was inaugurated in 1980. The carcasses of these carriers accounted for more than $2 billion in annual revenues and almost 50,000 jobs.

Even large shippers are not immune to the adverse effects of deregulation. Chief executive officers of 27 of the nation's largest coal companies have vigorously complained to President Reagan about the extraordinary increases in rail rates imposed under deregulation. For many public utilities, it is today less expensive to import coal from South Africa or Poland than to pay the exhorbitant freight rates demanded by the railroads.

The Reagan administration deserves some serious criticism for its pursuit of the well-intentioned [but ill-conceived] transportation policies inaugurated by the Carter administration. President Reagan's appointees to both the Civil Aeronautics Board [which regulated the airlines] and the Interstate Commerce Commission [which regulates the railroads and the motor carriers] have, in the whole, been champions of deregulation. Carter's appointees were no better.

Had the CAB implemented airline deregulation as Congress intended, far less suffering would have resulted. Congress, in promulgating the Airline Deregulation Act of 1978, insisted on a gradual transition period for deregulation—three years for routes [the points between which a carier may fly], and four years for rates. The transition was anything but gradual.

Without a serious re-evaluation of the erosion of public interest values which the nation has suffered since deregulation, the legacy of Jimmy Carter will long be with us, at least until planes begin to fall from the air, or until the transportation industry becomes as highly concentrated as the rest of industrial America.

Paul Stephen Dempsey is professor of transportation law at the University of Denver College of Law and a critic of transportation deregulation. He formerly served as attorney for the CAB and ICC.

The Denver Post/Thursday, September 4, 1986 5B

Deregulation's toll is rising

by PAUL STEPHEN DEMPSEY

THE BANKRUPTCY of Denver-based Frontier Airlines is but the latest chapter in an industry struggling in the turbulent headwinds of deregulation. Even deregulation guru Alfred Kahn admits the airline industry is becoming an "uncomfortably tight oligopoly" in the Darwinian marketplace of bankruptcies and acquisitions.

In the short run, deregulation has meant a more competitive marketplace, where consumers have been given a wider choice of price and service (mostly price) options. Braniff became the first major casualty of improvident management after deregulation, and its bankruptcy served as a warning to others. Carrier management and labor, which had grown fat and lethargic under regulation, were forced to tighten their belts — to become lean, mean flying machines.

Lower ticket prices and increased industry productivity are considerable benefits of airline deregulation. But deregulation has not been without its costs.

Low fares have been distributed unevenly in favor of America's major cities, where the competition has been most intense for market share. But the empirical evidence suggests a positive correlation between higher ticket prices and fewer competitors. Transcontinental fares are sometimes lower than the price of flying to a small American city at less than half the distance away.

Passenger convenience has waned; today's traveler is flown on intensely packed aircraft funneled into congested hubs on flights that are chronically delayed, while he is served cardboard food. With all that, he feels lucky that he wasn't stranded by overbooking, as are many others less fortunate.

Stockholders and employees also have been stranded in the icy headwinds of deregulation. In the early years of deregulation, its advocates were slow to accept any blame, pointing fingers at the economic recession and wildly escalating fuel prices. But the recession hasn't reared its ugly head in a while and aviation fuel prices have been sent wildly crashing through the floor, as have wages for many employees.

Frontier's economic armageddon may be People Express's as well, for its founder, Donald Burr, suffers from the fatal flaw of the first of deregulation's airline mavericks, Sir Freddie Laker — excessively aggressive expansion. By purchasing Denver-based Frontier last year, Burr hoped to join the club of the four or five megacarriers that analysts predict will eventually dominate the industry. But Burr bit off more than he could chew in the hotly competitive Denver market, dominated by three major hub carriers — United, Continental and Frontier.

Burr was forced to reverse course, signing an agreement earlier this year to sell Frontier to the industry behemoth, United. The United purchase fell through and People put Frontier into bankruptcy as a tourniquet to stop the hemorrhaging of losses totaling $30 million a month.

Although United failed to acquire Frontier, it had already purchased many of its aircraft, hangars and gates at Denver. As the nation's largest airline and the premiere industry proponent of deregulation, it is vertically and horizontally integrated into a megacarrier that owns Westin Hotels and the Apollo computer reservations system, and has recently purchased Hertz Rent-a-Car as well as Pan American's transpacific routes.

How quickly will the industry come to be dominated by only a handful of airlines? Northwest Orient and Republic have just consummated the largest merger in aviation history. Texas Air (which owns Continental and New York Air) will likely refile its application with the Department of Transportation to acquire ailing Eastern Airlines (which purchased Braniff's South American operations upon the bankruptcy of that airline). TWA's application for acquisition of Ozark is also pending at DOT. TWA's owner, Carl Icahn, admits it will still need another merger partner if TWA is to be successful.

Together, Frontier's bankruptcy and these massive mergers will likely result in less competition and higher ticket prices at the hubs of Denver, Detroit, Minneapolis/St. Paul, New York, St. Louis and Washington, D.C.

These mergers and bankruptcies are not the last we will see. The weaker birds cannot fly in such fierce headwinds. Some will be consumed by larger predators. The skies of deregulation will get darker and stormier still before the dust settles on an industry dominated by giants.

The social Darwinists can celebrate the net result of deregulation. But we consumers have been taken for a ride.

Paul Stephen Dempsey is professor of law and director of the Transportation Law Program at the University of Denver

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AIRLINES

Consolidation a destructive trend

by PAUL STEPHEN DEMPSEY

THE REAGAN administration's Department of Transportation has approved every airline merger and acquisition proposal which has been submitted to it in the post-deregulation era. The list is dazzling.

It includes Texas Air's acquisitions of ailing People Express (and its subsidiaries, Britt, PBA and bankrupt Frontier Airlines) as well as anemic Eastern Airlines. Frank Lorenzo's Texas Air (which also controls Continental, New York Air and Rocky Mountain Airways) emerges as the largest airline company in the free world. Only the Soviet Union's Aeroflot flies more aircraft.

It also includes United's purchase of Pan American's transpacific operations, Northwest's acquisition of Republic and TWA's purchase of Ozark. DOT is likely to approve the proposals of Delta to acquire Western, and of American to acquire AirCal.

When the dust settles, the five largest airlines in the nation will control more than 80 percent of domestic capacity; the top seven carriers will account for nearly 85 percent of revenue passenger miles. Worse still, several of America's major transportation hubs are now dominated by a single airline, which accounts for more than 50 percent (in some instances, 80 percent) of market share. These include Detroit, Minneapolis/St. Paul, Newark, Pittsburgh, St. Louis and Salt Lake City. And Denver's three-carrier hub competition is reduced to two with Texas Air's acquisition of bankrupt Frontier Airlines.

In earlier days, deregulation proponents emphasized the discount fares stimulated by Sir Freddie Laker's Skytrain, Ed Acker's Air Florida or Donald Burr's People Express. But like 150 other airlines, these have been blown from the skies by the unfriendly headwinds of deregulation. Like a man who created a Frankenstein's monster, deregulation guru Alfred Kahn now laments that the industry is becoming an "uncomfortably tight oligopoly."

But DOT, in approving all the mergers submitted to it, has vociferously insisted that new-carrier entry will re-establish competition lost as a result of concentration. In theory, if a producer of a commodity or service is earning super-competitive profits, new entrants should be attracted like sharks to the smell of blood.

Despite DOT's dogged optimism, America's monster airlines have too many advantages to be seriously threatened by new competitors. Let me examine a few of them:

✓ *Landing slots, gates and terminal facilities.* Incumbent airlines have consumed the infrastructure at America's major airports. Takeoff and landing ceilings exist at four of our nation's busiest airports — Chicago's O'Hare, Washington's National and New York's Kennedy and LaGuardia. At these airports, an incumbent airline can realize oligopoly rents by selling landing slots at a high premium, or by purchasing additional slots to increase its market power, thereby enabling it to raise ticket prices.

> "Ticket prices will rise while service declines."

In addition, 68 percent of the nation's leading airports have no terminal space available for new entrants. As a result of the recent mergers, TWA now controls more than 80 percent of the gates at St. Louis; Northwest controls a like number at Minneapolis/St. Paul. Such hub domination means that no new entrant can hope to match the incumbent's frequencies, or enjoy its capacity advantages or overhead passenger flow, even if it could find a few gates to lease. With the exception of Texas Air's most recent gluttonous feasts, DOT has failed to preserve competition by insisting that the merging enterprise surrender landing slots or gates to a competitor.

✓ *Computer systems.* Approximately 90 percent of travel agents book flights on computer reservations systems. United and American Airlines own the nation's two largest such systems, Apollo and Sabre, respectively. Although DOT regulations are designed to eliminate display bias in the systems, critics object to the advantages enjoyed by parent airlines.

A sophisticated computer system enables the airline that owns it to target promotional fares at only the number of passengers needed to fill seats. It can respond daily (even hourly) to market demand and competitors' pricing maneuvers, and thereby maximize revenue. Among the reasons that People Express disintegrated was that it had no such system.

✓ *Frequent flyer programs.* The business passenger, whose demand is less price-elastic than the vacation traveler, is the most lucrative member of the air passenger market. The larger airlines are able to build brand loyalty among businesspeople, not only with their superior ability to serve major geographic regions, but also by offering free travel to exotic destinations as a reward for accumulating mileage.

✓ *Labor Costs.* In the early years of deregulation, new entrants were able to offer relatively low fares reflecting their lower labor costs. But since then, the incumbent airlines have renegotiated union contracts to improve productivity and reduce salaries. Carriers such as United and American now have two-tier pay scales, with still lower wages for newly hired employees. Thus, the competitive cost advantages once held by new entrants have largely evaporated.

✓ *Investor confidence.* With 150 airlines having gone "belly up" since deregulation began, the capital markets for new ventures are drying up. The airline industry is more susceptible to distress-sale pricing than most, for it produces an instantly perishable commodity. Once an aircraft taxis down the runway, empty seats are lost forever — they cannot be warehoused and sold another day, as can, say, canned beans. Thus, the vicissitudes of the marketplace are particularly brutal in transportation. The giants of the industry, with their deeper pockets, can better weather the storms of a turbulent economic environment.

The bottom line is this: The headwinds of deregulation are particularly fierce for small entrepreneurs; while we may have a few strong, but relatively small, regional airlines flying about in these unfriendly skies, the megatrend of deregulation appears to be an oligopoly of megacarriers. With the market power engendered by increased concentration, ticket prices will rise while service declines. Wealth will be transferred from consumers to producers, and society's resources will be misallocated.

The Reagan administration's antitrust policy is the most permissive since the Sherman Antitrust Act became law in 1890. No prior administration would have approved concentrations of this magnitude, in this or any other industry. Hence, larger carriers are scrambling to devour the smaller ones while the candy store is open. In this social Darwinist environment, one shouldn't be too surprised if Frank Lorenzo makes an offer to purchase the U.S. Air Force, and DOT approves it.

Paul Stephen Dempsey is professor of law at the University of Denver College of Law.

USA TODAY ®

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Chairman and Founder
Sept. 15, 1982

John C. Quinn
Editor

John Seigenthaler
Editorial Director

OPINION

The Debate: UNFRIENDLY SKIES

PAUL STEPHEN DEMPSEY
Guest columnist

Consumers pay more to receive a lot less

HANOVER, N.H. — Airline deregulation has had nearly a decade to prove its superiority to the system it replaced. In the short run, fares fell as carriers battled for market share. In the longer run, bankruptcies and mergers have created what Alfred Kahn describes as an "uncomfortably tight oligopoly." A half-dozen megacarriers now dominate more than 80 percent of domestic traffic. And air service has, quite simply, gone to hell.

Today, we are herded aboard crowded aircraft, flown through congested skies into hub-and-spoke bottlenecks, fed cardboard food, overbooked, bumped and misconnected, and required to sleep in strange cities on Saturday nights, all for a non-refundable discount ticket and a few frequent-flyer miles.

While ticket prices have fallen for some consumers, business and small-community travelers are denied most discounts. More than 100 small towns will disappear from the air-route map next year when federal subsidies expire.

But even consumers who pay a lower ticket price are incurring additional costs for a demonstrably poorer product. We pay in consumption of time and money and increased levels of anxiety for late arrivals and departures, missed connections, the search among a bewildering array of fares, lost baggage, circuitous routing, and a decreased margin of safety. Communities and airports pay with declining property values. If we could measure all these expenses in dollars, we would have a clearer picture of the costs and benefits of deregulation.

The Department of Transportation holds ample jurisdiction to protect consumers against market abuse and industry concentration. But with its infatuation with laissez faire, it lacks the will to do much of either. Secretary Elizabeth Dole has announced a few modest sanctions, only as her husband approaches the presidential-campaign trail.

New legislation is needed to correct the most egregious carrier practices, including unrealistic scheduling of more flights than airports can possibly accommodate; deliberate overbooking, where more tickets are sold than available seats; and bait-and-switch advertising, where the advertised discount is available only on a few seats which are sold before many customers call. Such jurisdiction must be vested in an agency other than DOT, which has shown itself incapable of protecting the public interest.

Not since 19th century courts embraced the doctrine of *caveat emptor* (let the buyer beware) have we lived in an environment where those without equality of bargaining power could be so easily exploited

Paul Stephen Dempsey is director, University of Denver Transportation Law Program.

Fear of Flying Frequently

The hub system has caused the airways to become more crowded than they ever were

BY PAUL STEPHEN DEMPSEY

Ten years ago flying was a relatively civilized experience. The airways and airports were not as congested as they are now—and we could often fly to our destinations nonstop. But getting from here to there is much more difficult today. Except for flights between major cities, air travel is almost certain to mean a change of planes at a hub airport. Fly south on Delta or Eastern, and change planes in Atlanta. Fly west on Continental or United, and change planes in Denver. Fly to the Midwest on United or American, and change planes in Chicago. Fly northwest on Northwest, and change planes in Minneapolis or Detroit. As we enter the 10th year of airline deregulation, the hub-and-spoke system of distributing passengers has been adopted by every major airline. And this structural shift in scheduling has become a major, if underreported, cause of chaotic conditions in the air-traffic system.

Under hub-and-spoke routing, a carrier funnels its aircraft into a single airport, then herds its passengers onto connecting flights in a series of steps that depends on tightly scheduled arrivals and departures. If a plane is late, as many are these days, passengers won't make their connections. The lucky ones will be booked on a later flight; the less fortunate will spend the night in airport hotels. Businessmen desperately seeking to get to an important meeting become nervous and angry; so do airline employees trying to sort through the mess of late or canceled flights. At times, the hub airport takes on the qualities of a meatpacking house.

Being funneled through a hub also means more hours en route. Not only must prudent passengers count on spending at least an hour between arrival and departure in order to make a connection, but they will also spend more time in the air because of the circuitous routing mandated by this new system. Instead of being flown from A to B, as was the case before deregulation, passengers are now flown from A to C, where they change planes for B. The trip from Grand Forks, N.D., to Seattle, Wash., requires a flight east to Northwest's hub in Minneapolis. And the only way to fly from Cheyenne, Wyo., to Caspar is by way of Denver—more than double the air miles from point to point. Under the hub system, the distance between two points is rarely a simple straight line.

A decade ago the proponents of deregulation assured us that if we freed the airlines from the shackles of government, consumers would enjoy a utopia of price and service competition. But the promised paradise never arrived. Indeed, with the unprecedented wave of mergers and acquisitions that followed deregulation, the airline industry has evolved into an oligopoly. Today six megacarriers transport more than 80 percent of the nation's domestic passengers. And several hubs have become virtual monopolies:

- More than 80 percent of the traffic at each of three different airports—Minneapolis/St. Paul, Pittsburgh and St. Louis—is handled by a single airline: Northwest, USAir and TWA, respectively.
- More than 60 percent of the air traffic at hubs like Charlotte, Detroit, Newark and Salt Lake City is controlled by a single airline—by Piedmont, Northwest, Continental / Eastern (Texas Air Corp.) and Delta.
- At some airports, two airlines control more than 70 percent of the market. Delta and Eastern are duopolies in Atlanta; United and American dominate Chicago, while Continental and United rule Denver.

Because the incumbent airlines have monopolized the infrastructure of landing slots, gates and other terminal facilities, "fortress hubs" become impenetrable to new competition. It should come as no surprise then that ticket prices are rising and restrictions on discount fares are being tightened. The equation is simple: the stronger an airline's hub, the greater the opportunity to raise prices on its spokes. TWA's flight from its hub in St. Louis, Mo., to Madison, Wis., takes only an hour, but can cost $225 one way. Yet its flight from New York to Los Angeles, via St. Louis, costs $199.

Despite inconveniences to passengers, airlines find the hub-and-spoke system profitable. It allows them to multiply the number of cities they can serve—and to fly planes that are more than half full instead of more than half empty as they did on some nonstop routes. More flights to more cities give an airline more flexibility in its routes, more marketing opportunities and the traffic needed to dominate the hub.

Hubs and spokes have changed the structure of scheduling aircraft but, by multiplying the number of takeoffs and landings, they have caused the airways to become more crowded than they were before. Couple this with the desire of each airline to serve the businessman's peak-demand times and the traffic problems are compounded by what transportation experts call the "waves" of aircraft scheduled in and out of a hub during the early morning and late afternoon. Too many aircraft passing through too narrow a window of time and space means frequent passenger delays and missed connections, not to mention an erosion of the safety margin.

The air-traffic system is just not able to handle the congestion created by the hub system. And the fact that the government has not restaffed the control towers to the levels before the air controllers' strike of 1981, or updated the FAA's outdated equipment, only exacerbates the structural problems hubs have caused.

Flying is such a stressful experience today that it is easy to forget how we used to get from here to there. We once had a coordinated system of national transportation that allowed us to get from point to point at a fair price and in reasonable comfort, without traveling halfway to hell and back. Deregulation has given us the worst of all worlds—a significant deterioration in the quality of service provided by a handful of huge firms that are now raising prices as they funnel America through "hub and choke" bottlenecks. We deserve better.

Dempsey is director of the transportation-law program at the University of Denver College of Law.

Sun., May 25, 1986, Denver, Colo. Rocky Mountain News

Deregulated skies unfriendly to small airlines

by Paul Stephen Dempsey

THE recent acquisition of Denver-based Rocky Mountain Airways by Continental Airlines is but the latest hapter in the increasing trend toward concentration in the eregulated airline industry. Indeed, a growing number of maller and unhealthy carriers are flying into the turbulent kies of deregulation, only to be gobbled up by the indus-ry's giants.

If unconditionally approved by the U.S. Department of ransportation, the pending acquisitions of Eastern by Tex-s Air, of Republic by Northwest Orient, and of Ozark by WA will signal the beginning of the end of the vigorous ricing competition that many consumers have enjoyed in ur nation's largest passenger markets since the late 1970s.

Frank Lorenzo's Texas Air has been vigorous in its fforts to acquire airlines ailing in the fierce headwinds of eregulation. He succeeded in his hostile takeover of Conti-ental, then rammed the carrier through Chapter 11 bank-uptcy to shed himself of its union contracts.

Last year, Lorenzo failed in a $793.5 million bid for Trans /orld Airlines. But this year he succeeded in a $675 million erger agreement with Frank Borman's anemic Eastern irlines. Lorenzo inherits Eastern's $2.5 billion debt as well s a $9.5 million fine imposed by the Federal Aviation dministration for 73,373 alleged safety violations.

A merged Texas Air-Eastern may become the largest irline in the United States. It would also dominate the crative New York-Washington shuttle service, which has eretofore been highly competitive.

TWA avoided Lorenzo's frontal assault, but was subse-uently devoured by corporate raider Carl Icahn. This year, Icahn consummated an agreement to purchase Ozark Air Lines for $250 million. Both TWA and Ozark operate hubs at St. Louis. The combined carriers would control 56 of the 74 available gates at Lambert International Airport.

Also this year, Northwest Orient announced plans to swallow Republic for $884 million. A merged Northwest Orient and Republic would become the third largest U.S. airline. The Justice Department alleges that competition could suffer in some 85 markets.

Hence, these three mergers portend reduced competition at the major U.S. hubs of New York, Washington, St. Louis, Minneapolis/St. Paul and Detroit. Over 60% of American airports have no available gate space for new entrants.

In the years immediately after promulgation of the Airline Deregulation Act of 1978, there was a similar rash of merger activity. North Central Airlines and Southern Airways joined to become Republic Airlines in 1979, and acquired Hughes Airwest the following year. Pan American World Airways acquired National.

More recently, the industry behemoth, United Air Lines, bought half of Frontier's 50 aircraft and Hertz Rent-a-Car.

Last fall United bought all of Pan Am's trans-Pacific routes, corresponding aircraft and ground facilities for $750 million. What was left of Frontier was picked up by Donald Burr's aggressive People Express, the only new major entrant into the industry since deregulation.

There is speculation that still more airline mergers may be in the offing as obesity becomes epidemic. A continuation of consolidations and acquisitions could well reduce the industry to one dominated by only four or five megacarriers within a few years.

Concentration through mergers and bankruptcies is the inevitable consequence of the competitive market forces unleashed by deregulation. The airline industry is more subject to distress-sale pricing than most, for it markets product that is, in essence, an instantly perishable commo ity. Once an aircraft rolls down the runway, any emp seats are lost forever; they cannot be warehoused and so another day like, say, canned beans.

In an era of distress-sale pricing, carriers without dee pockets (e.g., United) or extremely low costs (e.g., Peopl become candidates for bankruptcy or acquisition. In an er of lax antitrust enforcement, oligopoly may be the ultima result of this trend, as stronger carriers drive out th weaker through a social Darwinist process of predato pricing. Those not driven out are swallowed up through th increasingly popular process of mergers and acquisitions

Consolidations will inevitably reduce competition i many markets, thereby forcing fares up. However, th airline industry's profitability (and, it is hoped, its margi of safety) will improve.

The traveling public deserves a safe, efficient an healthy airline industry that provides adequate service at reasonable price. With the demise of the Civil Aeronautic Board mandated by the Airline Deregulation Act of 197 government no longer assures that these public-interes values will be protected.

In the absence of economic regulation, only responsibl enforcement of our antitrust laws will ensure that consum ers continue to enjoy the efficiencies and economies of competitive marketplace, and that they will be protecte against the extraction of monopoly or oligopoly profits.

It was Adam Smith who recognized that the market wil remain free only at governmental insistence.

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Commentary

Deregulation stranding residents of the lone prairie

/ Paul Stephen Dempsey

TRAILWAYS, whose buses serve more Colorado communities than any other passenger carrier, has decided abandon the entire state. Trailways plans to terminate rvice to many surrounding Rocky Mountain and western tins states as well, including Wyoming, Nebraska, Montana, South Dakota and much of Kansas.

Greyhound, too, has taken the opportunity afforded it by e Bus Regulatory Reform Act of 1982 to abandon many all towns in this part of the country. The bankruptcy of ontier Airlines further contributes to rural isolation, as ssenger service is suspended between Denver and many ocky Mountain communities. Under deregulation, transrtation to points in rural America is disintegrating.

Economic regulation was by no means a perfect system. o often slow and cumbersome, it frequently lacked foreght and innovation. It sometimes bred lethargy and inefficency among management and labor. Such is the price we y for turning over decisions to a government dominated political patronage at the top, and excessive job security nong the rank and file.

But regulation protected public-interest values that ight not find a high priority in the marketplace. It treated mmon carriers (bus, truck, railroad and telephone comnies) as industries with a unique responsibility to satisfy e needs of the public for universal service at just and asonable rates. Small communities as well as large (and nall shippers as well as large) were required by federal d state regulations to be served reasonably well and at a n-discriminatory price.

Regulation imposed upon common carriers both a burden d a benefit. The burden was the obligation to provide an lequate level of service to all geographic areas within eir operating license, at reasonable prices. Inadequate rofits earned from the small were cross-subsidized interally by more than adequate profits earned from the large. In return, the regulated enterprise was granted a franchise that shielded it from predatory competition of the kind that drove Frontier Airlines into bankruptcy.

Economists argued that this transfer of wealth from urban to rural communities, and from large shippers to small businesses, created a misallocation of resources. The unregulated marketplace would better allow each consumer to enjoy that price and service dictated by the laws of supply and demand. Such was the conventional wisdom that brought about deregulation.

Why treat transportation differently from other industries?

If transportation were like other industries, we would leave all aspects of it to the marketplace. We would have government stop building roads and highways and leave their construction to private entrepreneurs who could exact tolls on their use.

> If we are one nation, we in urban areas must be concerned with ... our rural neighbors.

Under an approach that relied exclusively on the marketplace, the U.S. Postal Service would be abolished and letters would be delivered, if at all, by private companies at whatever price the market would bear. We would end subsidies to public urban transit, allowing private enterprise to take over those routes that could turn a profit and abandon the rest.

But the social costs to the poor and the elderly, who would have to fend for themselves (either by walking or hitchhiking), and the congestion, environmental pollution, and stagnation of commerce created by such irresponsibility would be enormous.

The World Bank provides loans to Third World nations to develop transportation and communications because it recognizes that economic growth is unattainable without them. Sri Lanka can secure a loan for construction of a railroad o a telephone system because the World Bank realizes tha these are the foundations of prosperity, and addition economic growth will be built on top.

The same reality confronts rural regions of the Unite States. Transportation is essential to economic growt Without it, rural areas will never realize the America dream of employment and prosperity. This was the ratic nale upon which public-interest regulation was predicate

Telephone regulation was imposed to ensure that a communities in the nation, no matter how small or remot enjoyed "universal service." Long-distance profits cros subsidized local-service losses. Deregulation and the breal up of AT&T reversed this process. As a consequence, loc telephone rates are forced to rise.

As Frontier folds, Greyhound retrenches and Trailwa abandons much of the West, it becomes increasingly dif cult to get there from here. And, under the provisions of t Airline Deregulation Act of 1978, the problem will exacerbated; federal subsidies that support what is left air service to small communities will expire in 1988.

Ultimately, those without the private automobile will left stranded. The economic base of isolated communiti will become more difficult to sustain.

If we are one nation, we in urban areas must be co cerned with the plight of our rural neighbors. If the n result of deregulation for our surrounding region is poor transportation and higher-priced communication service we are all worse off.

Denver is the heart of the largest rural basin in t United States. We in the West have a responsibility object to a policy that denies our region the foundation economic growth. Deregulation may have been a good th for many large businesses and large cities, but it is a ra deal for small business and rural America.

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OUTLOOK Items on this page do not necessarily reflect the opinions of the Houston Chronicle.

The carnage of airline deregulation

by Paul Stephen Dempsey

AIR TRAVEL IS BECOMING a decidedly less pleasant and more expensive adventure as deregulation nears the end of its first decade. The quality of life in airports has degenerated into that of a crowded stockyard on a muggy summer afternoon. The deregulated airline industry suffers from airport and airway constipation, poor returns on investment, the worst labor-management relations of any major American industry, a deteriorating margin of safety and a well deserved loss of consumer confidence.

Freed from regulation, the airline industry has massed into what economist and former Civil Aeronautics Board Chairman Alfred Kahn now admits is an "uncomfortably tight oligopoly." As the dust settles from an unprecedented wave of mergers, fewer than a half dozen gargantuan airlines now dominate more than 80 percent of the passenger market. One wonders whether the last coat of fresh paint on jets will have a chance to dry before the next acquisition is announced.

At a number of "fortress hubs," a single airline accounts for more than 60 percent of traffic. In order of concentration, these include St. Louis, Pittsburgh, Charlotte, N.C., Memphis, Minneapolis, Salt Lake City, both Houston airports, Detroit, Newark, N.J., and Dayton, Ohio. And, at the two-carrier hubs of Atlanta, Denver, Dallas/Ft. Worth and Chicago, the incumbent duopoly controls more than 70 percent of the market. So one should not be surprised that ticket prices are on the rise as carriers become more proficient at flexing their muscles of market power.

A regulated monopolist (such as our local telephone and electric companies) is prohibited from charging more than a just and reasonable rate. But free a monopolist from regulation, and it can charge whatever the market will bear. Fly to a small town if you want to experience the reign of an unconstrained monopolist. And with the airline industry becoming an oligopoly, ticket prices in larger markets are now climbing upward.

Led by Kahn, the economists who cleverly convinced Congress to deregulate the industry in 1978 dogmatically insisted that new rivals would spring out of the air to challenge the large incumbents. Under the "theory of contestable markets," new entry, or its threat, would keep the industry hotly competitive. New entrepreneurs would be attracted to markets in which incumbents were earning supra-competitive profits like sharks to to the smell of blood. Adam Smith's "invisible hands" would reach out from his grave and provide the level of price and service options dictated by consumer votes of dollar approval. And we would all live happily ever after.

But nearly a decade of empirical evidence strongly refutes the theory. Some 150 airlines, Houston-based TranStar the latest among them, have fallen from the unfriendly skies into financial trouble, unable to withstand the fierce competitive head winds which escaped from Pandora's box of deregulation. The smiling faces of Freddie Laker and Donald Burr will never again grace the cover of Time magazine. The fortress hubs have become impenetrable, as the industry's giants have consumed the infrastructure of gates and landing slots, and attained the significant network advantages of beyond-segment traffic flow.

The only new carriers to find a "niche" and escape the carnage of deregulation are those which have made peace with the big boys, becoming, in essence, their franchisees, feeding the large carriers' hubs with traffic from small communities, and painting their small planes in megacarrier colors. Who would have dreamed that survival of small airlines would come to depend upon being listed on the computer reservations screen as an on-line connection with one of the industry's behemoths?

Competition among large airlines appears merely to have degenerated into imaginative forms of consumer fraud. Freed from regulation, airlines deceive their passengers with unrealistic scheduling, deliberate overbooking, and bait-and-switch advertising. In June, more than 40,000 flights were delayed, for which consumers lost millions of dollars in opportunity costs. We wait for reservations agents to answer our calls (and tell us, "sorry the discount seats have all been sold"); we wait to check in, to board, to depart, to arrive; we wait at airports for our bags and for taxis; we wait and wait and wait.

Late departures too often mean missed connections in the "hub-and-choke" bottlenecks. Consumers are also left stranded by the industry's practice of deliberately overbooking flights and bumping the excess passengers. No one knows how much luggage has been lost, or how many tickets have gone unrefunded (either because the passenger changed his itinerary, or because bankruptcy grounded the carrier's aircraft). But one thing is certain; P.T. Barnum would be proud of the deregulated airline industry.

Freed from regulation, the industry has also trimmed its margin of safety. Some of that is attributable to cost cutting, as carrier profit margins have been sharply squeezed. Acquisitions, too, pose a problem as carriers attempt to digest unfamiliar aircraft and merge maintenance staffs and facilities. And with near misses soaring in these congested skies, the next aerial tragedy cannot be far beyond the horizon.

Consumer protection has largely been an anathema to the Department of Transportation, itself wedded to the deregulation dogma of the Reagan administration. As a consequence, passengers have few legal rights against deceptive carrier practices such as deliberate overbooking and misleading advertising. Merger applications have also been consistently approved by DOT, despite legitimate antitrust concerns. And the agency could be more vigilant in enforcing airline safety standards, and bringing air-traffic controller staffing up to pre-PATCO strike levels. Transportation Secretary Elizabeth Dole has recently taken a less ideological and more pragmatic stance against some industry abuses, but only, as it seems, as her husband, Sen. Robert Dole, R-Kan., approaches the presidential campaign trail.

The nation is poorly served by a transportation industry in chaos. The choice between imperfect competition and imperfect regulation is never an easy one. But the ideologues of deregulation have produced an intolerable level of turbulence in what once were friendlier skies. An increasing number of us who fly would gladly trade a little more government for a lot less chaos.

Dempsey, formerly an attorney with the Civil Aeronautics Board, is professor of law and director of the Transportation Law Program at the University of Denver College of Law. He is author of *Law and Foreign Policy in International Aviation*, due out this summer.

Airline safety victim of deregulation

Fewer traffic controllers, reduced maintenance contribute to problem

By PAUL STEPHEN DEMPSEY

Airline safety has taken a nose dive under deregulation. Witness the soaring number of near misses, the shoddy maintenance, and the sloppy landings. Observe the white-knuckled passengers tightly clinching their arm rests, and ask them whether deregulation has made the skies friendlier.

"Near misses" is an inaccurate term for what really are "near-hits." Not in the history of aviation have so many aircraft passed so uncomfortably close, with so little a margin for error. By funneling their flights into "hub and choke" bottlenecks, and scheduling takeoffs and landings through a narrow window of time, airlines have sent their fleets down arteries of coagulation.

Add to that the failure of the Federal Aviation Administration (FAA) to re-staff the air traffic control system to pre-PATCO strike levels, replace obsolete equipment, impose peak-period landing fees, or limit general aviation access, and you have a prescription for disaster.

Jimmy Carter's chairman of the Civil Aeronautics Board (CAB), Alfred Kahn, is the anointed father of deregulation. He insists that the skies have never been safer; America has never experienced fewer passenger fatalities. If the body count was the only measure of victory, we would have won the war in Vietnam.

But why not more crashes, then, if the margin of safety has eroded? Two reasons.

First, the redundancies built into over-engineered jets by manufacturers have made it possible to stay aloft even when aircraft are poorly maintained. If one system fails, the back-up will usually do the job.

Second, pilots know that maintenance and labor have taken a beating as carrier profit margins have plummeted. This has mandated a keen level of vigilence in the cockpit. Few of life's trials are as sobering as the fear of death. While we have recently been spared major crashes, we may be living on borrowed time. The next wave of aerial disasters cannot be far beyond the horizon. The recent carnage at Detroit, although apparently not attributable to deregulation, may be the harbinger of things to come.

Kahn also argues that economic regulation has nothing whatever to do with safety. The CAB, he insists, played no role in maintaining airline safety; that was the FAA's job.

It is doubtful that the economic health of carriers can ever be de-coupled from safety. It is no secret that

maintenance has deteriorated under deregulation, despite record fines imposed by the FAA. With more than 150 carriers having gone belly up under deregulation, and with industry profit margins so weak, some carriers simply cannot afford to take defective aircraft out of service. Witness the crash of ill-fated Arrow Air, when a jet full of American soldiers gave their lives for deregulation.

When the industry was healthier, it could afford a comfortable margin of safety above FAA minimums. But today, FAA standards have become the ceiling, rather than the floor. Prior to Kahn, the CAB recognized this principle, and devoted considerable energy to protecting the economic health of the industry. This policy manifested itself in several ways.

First, before a carrier was licensed to operate, the Federal Aviation Act required that it prove itself "fit, willing, and able" to provide the service safely. A grossly undercapitalized applicant could not demonstrate financial fitness, and therefore was denied the CAB's permission to fly. Second, where multiple applicants sought authority to enter lucrative markets, the CAB would often favor those banking regulatory agencies, the CAB would encourage a healthy suitor to acquire a company approaching the precipice of bankruptcy. This was how Delta acquired ailing Northeast Airlines in the early 1970s.

The Airline Deregulation Act of 1978 gutted much of the CAB's jurisdiction. Nonetheless, the statute's first two provisions reminded the agency that the promotion of safety should be a policy imperative of the highest priority, and that its deterioration should be prevented. Kahn tends to ignore the statutory language and four decades of agency precedent. But Kahn is an economist, not a lawyer. And economists, one soon learns, tend to perceive truth more clearly than the rest of us.

Imaginative arguments have been advanced to assuage the fear of flying in these unfriendly skies. One of the most cold-blooded is that the market will ultimately solve the safety problem. No airline can afford to have too many crashes, or the public will shy away from it. Remember the collision of an Air Florida jet with Washington, D.C.'s Fourteenth Street bridge? The picture of Air Florida's tail sticking out of the icy Potomac dominated the week's news, and the carrier was soon submerged in bankruptcy.

No one can quarrel with the basic economic principle that if an airline kills off its passengers, it won't have any. But the men and women who lost their lives in the Air Florida and Arrow Air disasters would likely have preferred government protection before they ascended into heaven. No doubt their souls gain little comfort in knowing that Adam Smith's "invisible hands" vindicated their deaths by strangling the economic life out of the unsafe airlines.

In a deregulated environment, we can no longer rely upon government to protect those of us who fly. We can only pray that the airline industry isn't on a collision course. Keep your seat belts fastened folks, because we're experiencing a little turbulence in these deregulated skies. Cross your fingers, and hope not to die!

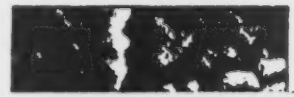
Dempsey is professor of law and director of the transportation law program at the University of Denver. He is author of the book *Law & Foreign Policy in International Aviation*, to be published in September.

A time of dishonor on the federal bench

Is the IRS opening your mail?

By BOB KRUEGER

The truth in the old saw "Nothing is certain but death and taxes" reminds us that, like the poor, undertakers and tax collectors are always with us. The certainty of their professions' continuance has never won them widespread popularity, of course.



Hobart Rowen

Washington Post July 23, 1987 at A21

'Airline Service Has Gone to Hell'

In Chicago the other evening, after all passengers were seated on an American Airlines flight to National Airport, a stewardess' voice came over the speaker system: "Sorry to be the bearer of bad news, ladies and gentlemen, but we have an equipment malfunction, and we won't know for 30 minutes whether this flight will go."

There wasn't a passenger on that flight who didn't observe that the news of the potential cancellation had been delayed until all were aboard—when it was too late to catch a United Airlines flight due to take off for Washington at about the same time.

And how many times have you called an airline to book a flight at an advertised bargain price to be told: "Sorry, there were just a limited number of seats available at that price, but we can let you have . . ."

"When you deal in goods, that would be called 'bait-and-switch' advertising under the antitrust laws," said University of Denver transportation-law expert Paul Stephen Dempsey. "But under deregulation, the airlines get away with it."

It has been apparent to many for some time that the effect of airline deregulation is to let the industry drift into the dominance of a handful of companies, each ruling the roost out of a regional "hub."

Deregulation in fact has been a disaster, as is now belatedly recognized by The Wall Street Journal, which Monday featured a detailed story headed: "An Unexpected Result of Airline Decontrol Is Return to Monopolies." The subheads told the rest of the story: "Big Carriers Are Dominating Nation's Hub Airports; Legislators Are Concerned—Higher Fares and Less Service."

As stronger carriers gobbled up competitors through bankruptcies and mergers, a handful of giants has emerged: if you are in Minneapolis or Milwaukee, you have little choice except to fly Northwest. In St. Louis, Trans World Airlines is kingpin, with 317 departures compared with 22 for its nearest rival, Southwest Airlines. In Dallas, it's American Airlines. In Pittsburgh, it's USAir, and so on. According to Dempsey, Texas Air, United, Delta, American, TWA and Northwest control more than 84 percent of passenger traffic, up from 73 percent before deregulation.

Moreover, 148 small cities now have assurance of some airline service with the help of federal subsidies, provided in a 10-year phase-out period under the 1978 deregulation act. That will come to an abrupt end next year. Dempsey said in an interview that his guess is that 100 of those towns will soon have no air service at all. (As it is, most small cities under deregulation are served by commuter lines, whose safety record is inferior to that of the regular lines.)

Experts such as Dempsey, the late Civil Aeronautics Board chairman Secor Browne and Frederick Thayer of the University of Pittsburgh, among others, years ago predicted airline deregulation would degenerate into an airline oligopoly.

But Congress and the Carter and Reagan administrations instead listened to the siren song of deregulators, led by Alfred Kahn, Carter's CAB chairman. They promised that the "free market" under deregulation would stimulate competition, thus work to the benefit of consumers.

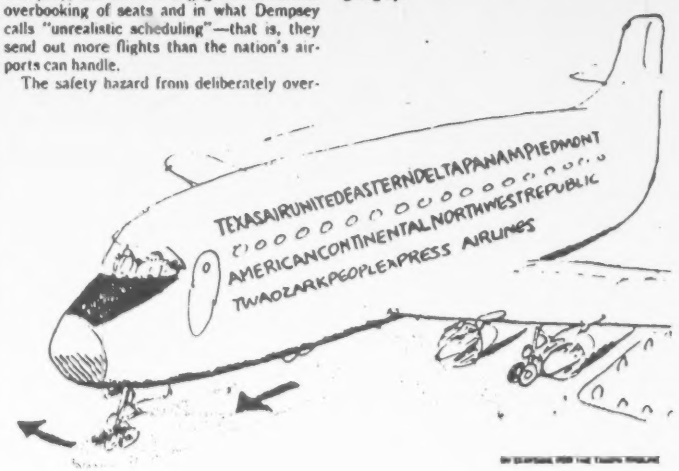
Back in 1983, David B. Richards of the CAB staff warned Congress that the short-term benefits of fare wars accompanying the early years of deregulation were disguising the potential longer term problems. But few paid attention.

Without the government looking over their shoulders, airlines have been free to abandon unprofitable routes, without regard to the impact on the local populace or industries; manipulate fares up and down to attract business; use cutthroat competition—or unfair pricing—to force competitors to the wall. There really is no mystery about it: deregulation had had the same effect on the railroads and the trucking industry.

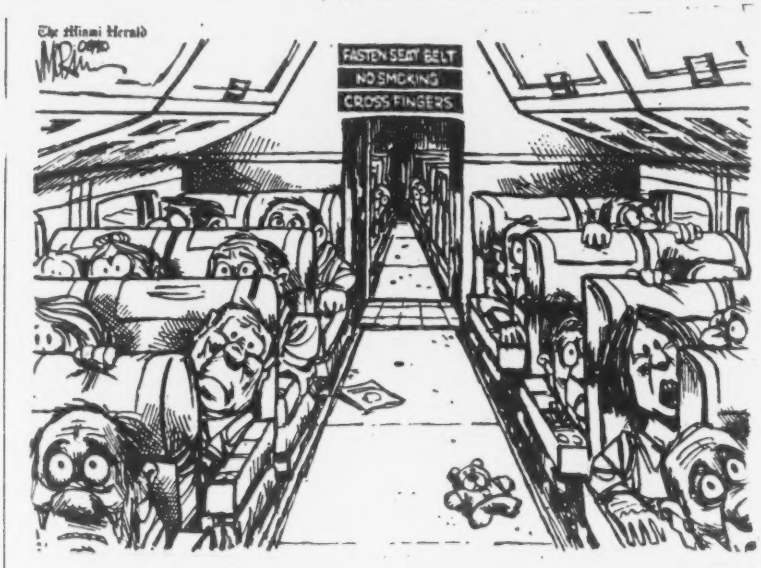
Even without regulation, the Department of Transportation still has authority to provide some consumer protection. But Secretary Elizabeth Dole seems to have little inclination to do so. In addition to the bait-and-switch advertising mentioned by Dempsey, the airlines engage in deliberate overbooking of seats and in what Dempsey calls "unrealistic scheduling"—that is, they send out more flights than the nation's airports can handle.

The safety hazard from deliberately overcrowding the airways is obvious. Usually, the carriers lay the blame for delays on the unseen and much-maligned air-traffic controllers. But as the captain of a recent Eastern Airlines shuttle said as he zoomed up to the New York area from Washington, only to be held in a pattern near LaGuardia Airport, "We're going to be stuck here for at least a half-hour. That's deregulation for you, folks!"

The time has come to reexamine Alfred Kahn's grand experiment. Deregulation does not work: airlines, like other forms of transportation, require economic regulation. To believe otherwise is to ignore reality. Airline service has gone to hell, and ticket prices are going up!



28 Section 1 Chicago Tribune, Friday, August 28, 1987



Cross your fingers, hope nct to die

By Paul Stephen Dempsey

Airline safety has taken a nose dive under deregulation. Witness the soaring number of near misses, the shoddy maintenance and the sloppy landings. Observe the white-knuckled passengers gripping their arm rests, and ask them whether deregulation has made the skies friendlier.

"Near misses" is an inaccurate term for what really are "near hits." Not in the history of aviation have so many aircraft passed so uncomfortably close, with so little margin for error. By funneling their flights into "hub and choke" bottlenecks, and scheduling takeoffs and landings through a narrow window of time, airlines have sent their fleets down arteries of coagulation.

Add to that the failure of the Federal Aviation Administration to restaff the air traffic control system to pre-PATCO strike levels, replace obsolete equipment, impose peak-period landing fees or limit general aviation access, and you have a prescription for disaster.

Jimmy Carter's chairman of the Civil Aeronautics Board, Alfred Kahn, is the anointed father of deregulation. He insists that the skies have never been safer; America has never experienced fewer passenger fatalities. Yet if body count were the only measure of victory, we would have won the war in Vietnam.

Why not more crashes, then, if the margin of safety has eroded? Two reasons. First, the redundancies built into over-engineered jets by manufacturers have made it possible to stay aloft even when aircraft are poorly maintained. If one system fails, the back-up will usually do the job.

Second, pilots know that maintenance and labor have taken a beating as carrier profit margins have plummeted. This has mandated a keen level of vigilance in the cockpit. Few of life's trials are as sobering as the fear of death.

While aviation disasters have not skyrocketed since deregulation, we may be living on borrowed time. The recent carnage at Detroit may be the harbinger of things to come. The next wave of aerial disasters cannot be far beyond the horizon.

Kahn also argues that economic regulation has nothing whatever to do with safety. The CAB, he insists, played no role in maintaining airline safety; that was the FAA's job.

It is doubtful that the economic health of carriers can ever be decoupled from safety. It is no secret that maintenance has deteriorated under deregulation, despite record fines imposed by the FAA. With more than 150 carriers having gone belly-up under deregulation, and with industry profit margins so weak, some carriers simply cannot afford to take defective aircraft out of service. Witness the crash of ill-fated Arrow Air, when a plane full of American soldiers gave their lives for deregulation.

When the industry was healthier, it could afford a comfortable margin of safety above FAA minimums. But today, those standards have become the ceiling, rather than the floor. Prior to Kahn, the CAB recognized this principle, and devoted considerable energy to protecting the economic health of the industry. This policy manifested itself in several ways.

First, before a carrier was licensed to operate, the Federal Aviation Act required that it prove itself "fit, willing and able" to provide the service safely. A grossly undercapitalized applicant could not demonstrate financial fitness, and therefore was denied permission to fly. Second, where multiple applicants sought authority to enter lucrative markets, the CAB often would favor those most in need of economic assistance. Third, like the banking regulatory agencies, it would encourage a healthy suitor to acquire a company approaching the precipice of bankruptcy. This was how Delta Air Lines acquired ailing Northeast Airlines in the early 1970s.

The Airline Deregulation Act of 1978 gutted much of the CAB's jurisdiction. Nonetheless, the statute's first two provisions reminded the agency that the promotion of safety should be a policy imperative of the highest priority, and that its deterioration should be prevented. Kahn tends to ignore the statutory language and four decades of agency precedent.

Imaginative arguments have been advanced to assuage the fear of flying nowadays. One of the most cold-blooded is that the market will ultimately solve the safety problem. No airline can afford to have too many crashes, or the public will shy away from it. Remember the collision of an Air Florida jet with the 14th Street bridge in Washington? The picture of Air Florida's tail sticking out of the icy Potomac dominated the week's news, and the carrier was soon submerged in bankruptcy.

No one can quarrel with the basic economic principle that if an airline kills off its passengers, it won't have any. But the men and women who lost their lives in the Air Florida and Arrow Air disasters would likely have preferred government protection before they ascended into heaven. No doubt their soul gain little comfort in knowing that Adam Smith's "invisible hands" vindicated their deaths by strangling the economic life out of the unsafe airlines.

In a deregulated environment, we can no longer rely upon government to protect those of us who fly. We can only pray that the airline industry isn't on a collision course. Keep your seat belts fastened, folks. We're experiencing a little turbulence. Cross your fingers, and hor to die.

Paul Stephen Dempsey is professor of law and director of the Transportation Law Program at the University of Denver, and a former attorney with the Civil Aeronautics Board. His book, "Law & Foreign Policy in Inte. ational Aviation," is to be published in

The CHAIRMAN. Thank you, Mr. Dempsey, your statement was very insightful. Let me start with you. What is a solution? Is a solution the cross-subsidization that previously occurred, or is the solution boosting EAS? Any thoughts?

Mr. DEMPSEY. I have five suggestions for legislation. One, I think——

The CHAIRMAN. You came prepared.

Mr. DEMPSEY. Yes, sir. I do think that section 419 subsidies, at the very least, should be continued beyond their expiration date next year.

The CHAIRMAN. That is going to be on the Floor in about an hour.

Mr. DEMPSEY. I hope that you vote for it. I am sure you will.

The CHAIRMAN. I am a sponsor of the bill.

Mr. DEMPSEY. I think that those subsidies need to be expanded to include essential bus service. I think that small towns are also reeling from the impact of bus deregulation. As I said, 4,500 small towns have lost bus service since 1982, when Congress passed the Bus Regulation Act of that year.

Second, there needs to be increased consumer protection legislation; and third, increased safety regulations. The Department of Transportation, although it has plenty of jurisdiction to clean up the industry, is doing a particularly poor job in these fields. It has jurisdiction under section 411 of the Federal Aviation Act to prohibit airlines from engaging in unfair and deceptive methods of competition. But it does almost nothing.

It has jurisdiction to regulate landing slots at airports. At the Nation's four busiest airports, DOT has simply put them up for auction. This has enabled the largest carriers to intensify their oligopoly presence in the major airports.

Fourth, the Department of Transportation should be divested of jurisdiction over regulatory affairs involving aviation. It has shown itself unwilling and incapable of doing an adequate job of protecting the government. It has approved every merger which has been filed with it since it acquired that jurisdiction from the Civil Aeronautics Board.

It is my very strongly felt opinion that no executive branch agency should have that kind of power. That kind of power should be vested in an independent regulatory commission outside the executive branch.

The CHAIRMAN. Another Civil Aeronautics Board?

Mr. DEMPSEY. Well, I would suggest that Congress take the remaining jurisdiction existing in the International Commerce Commission for surface transportation and in the Federal Maritime Commission for ocean shipping, and create a new Federal transportation commission, sweeping all the remaining regulatory functions into a single Federal transportation commission. Then you would have autonomy from the executive branch, and hopefully, a less ideological agency.

Finally, I think that the Robinson-Patman Act should be amended to prohibit pricing discrimination in the sale of services. At the time the Robinson-Patman Act was passed in the early part of this century, the service economy was not a major part of our economy. Ours was in an economy dominated by the sale of goods the legisla-

tive history of the Robinson-Patman Act suggested that Congress did not feel it necessary to prohibit service discrimination because the regulatory agencies did that quite well, particularly for the infrastructure industries.

Railroad discrimination was prohibited by the ICC at the time. Subsequently, the CAB was given jurisdiction to prohibit pricing discrimination for airlines.

The CHAIRMAN. Would that prevent higher density urban routes from obtaining some of the freight for the low density rural routes?.

Mr. DEMPSEY. It would prohibit discrimination between classes of passengers on the same aircraft. It would not prohibit discrimination in terms of flights going to a small vis-a-vis a large community.

The CHAIRMAN. How do we essentially get better service for the smaller communities? You, seem to be leaning toward returning to some form of cross-subsidization. Is that an accurate or inaccurate statement; or do you have any other ideas?

Mr. DEMPSEY. My hunch is that all of these things that I have suggested will be Band-Aids, and the problem is more severe than these solutions can really rectify.

I anticipate that Congress will ultimately conclude that there is a need to regulate monopoly transportation services. Monopoly transportation services are, these days, operations flowing in and out of small communities from hub airports where the incumbent airline can charge whatever the market will bear.

There may be a need for some re-regulation of some sort. And, if Congress cannot come up with the money for the subsidy, perhaps some re-introduction of regulation may be required to reinstate the cross-subsidy that small communities enjoyed before deregulation.

The CHAIRMAN. Mr. Nance, very briefly, could you give me a little more flavor of safety issues as they apply to smaller airlines?

Mr. NANCE. We just do not have the equipment to work with. You do not have the training, the companies do not have the money, they do not have the experience and the management staff. Too often, there is such a thin management structure that when the boss gets upset because the bottom line is decreasing, that upset will go immediately to the minds of the pilots and managers over them.

That means you get up to and including the situation where some manager puts his finger in a young pilot's face and says, son, either get that airplane off the ground or you're fired.

The CHAIRMAN. Do you think those pressures are even greater in the smaller airlines than there might be for larger ones? Not long ago Senator Hollings had a hearing where Eastern Airlines pilots testified that they are feeling pressure by management to take unsafe actions.

Mr. NANCE. There is no question. I am not in the business of running any sort of a clearinghouse, but I get, as an author, an awful lot of input. I can tell you categorically that what I hear out there just raises my hair all the time. It has not diminished, as I was hoping the problem would.

It has, in fact in many cases, increased within the commuters and the regionals.

The CHAIRMAN. Thank you all very much. I appreciate your comments.

The next panel we have is with John Coleman, director of the office of EAS; Mr. Charles Cadwell, Deputy Chief Counsel for Advocacy for the SBA.

Mr. Coleman, Mr. Cadwell, thank you for coming. We have heard a lot this morning, and I know you have been here.

Mr. Coleman, why do you not begin first.

STATEMENT OF JOHN COLEMAN, DIRECTOR, OFFICE OF ESSENTIAL AIR SERVICE, DEPARTMENT OF TRANSPORTATION, WASHINGTON, DC

Mr. COLEMAN. Thank you, Mr. Chairman.

Mr. Chairman and Members of the Subcommittee, Assistant Secretary Scocozza has asked me to extend his sincere regrets that the press of business prevented his being able to be here this morning. However, I appreciate having the opportunity to appear today on Mr. Scocozza's behalf, as you study the effect of airline deregulation on rural communities.

This certainly is a critical consideration in any evaluation of this economic regulatory reform. However, since the aviation industry is made up of a complex system of interrelationships, I propose we begin with quick look at the big picture.

I will summarize the Assistant Secretary's written testimony this morning but a full text is available to this subcommittee. As you know, aviation operations were deregulated in 1978 and the changes brought by this policy shape today's market. The results? Nine years ago, approximately 39 commercial carriers were operating. A recent count estimates that 131 are now in service.

I am sure that you are familiar with the study conducted by the Brookings Institution which concluded that today airline travelers in the United States are enjoying $6 billion per year in lower fares and more frequent flights.

Since 1978, the number of passenger enplanements has grown by over 140 million—a 55 percent increase.

Most important, Mr. Chairman, competition has been enlivened by deregulation. In fact, industry competition is more dynamic and diverse in its many elements today than ever before. Changing operating practices and marketing strategies are working to reshape the structure and business practices of the airline sector resulting in the greater competition which benefits the consumer, all consumers—rural and urban alike.

The press of competition has prompted the airlines to alter service patterns to meet consumer needs. Delivering what the consumer wants—including on-line services—has led to the development of business affiliations between major and regional carriers, and this phenomenon is reshaping small community air service.

Today, 45 of the 50 largest regional air passenger carriers which collectively fly more than 80 percent of those carried by regional operators, have entered into marketing alliances with one or more large jet operators.

Alliances between major and regional carriers can provide the rural area with substantial benefits, including integration of sched-

ules, cooperative marketing and promotional arrangements, participation by the regionals in the majors' frequent flyer programs, along with additional administrative and support services.

In 1978 not every State had regional or commuter service; today there are regional and commuter air carriers operating in each State. A recent study by the Department of Transportation revealed that, in fact, most States have experienced an increase in the number of regional/commuter carriers serving them. In addition, the industry fleet has grown substantially since 1978, both in overall number and in variety of sizes and types of equipment. This is a very key element.

Mr. Chairman, the general economic impact of airline deregulation on small and rural communities cannot be viewed separate and apart from the general economic conditions of a particular area. This is especially true when studying the health of areas dominated by agriculture and related industries.

As we consider the subject before us today, let us keep in mind that when Congress enacted the Airline Deregulation Act, it also acted to preserve air service to small communities. The sole purpose of the essential air service program was, and is, to guarantee continued access to rural transportation system by small and isolated points which had been a part of the air transportation network prior to deregulation.

There is no denying the fact, Mr. Chairman, that many of those communities not included under the EAS protective blanket lost service. However, the impact of these reductions was often cushioned by the availability of service at nearby airports.

It should also be noted here today that industry competition spurred by deregulation has prompted a decline in fares to markets of all sizes. While the decline in rural fares has been much more pronounced in major markets, such as large hub-to-large hub routes—where fares have declined by 17 percent on average—even in the smallest markets fares have declined an average of 7 percent.

The more modest fare reductions in smaller markets are not surprising. Traditionally, low density markets have had fewer fare and service options available. With a smaller base of consumers, it stands to reason that operating costs would be higher, service less frequent, and the fare structure tighter. Today's market simply reflects economic reality.

Whatever the disparity found between fare structures of large and small markets, the differences can be justified by cost analyses. Upon comparing costs with actual fares charged in various markets, it can be shown that the current pricing policies of commuter carriers are, in fact, quite reasonable.

For example, in 128-mile market with five passenger planes per day, the economic cost per passenger ranges from a low of $139 for an 8-seat aircraft to $322 for a 44-seat, F–27 aircraft. Thus, obviously, in order for a 128-mile market generating five planes per day, to support air service on its own without Federal subsidy, the one way fare would have to be well over $100.

Comparing this figure with various fares charged in essential air service markets, for example, we find Sky West charging $126 in

the Page to Phoenix, AR connection, a distance of 242 air miles with 13 enplanements per day.

Similarly in the Lamar-Denver market, a distance of 166 miles with four enplanements per day, Air Midwest is charging $119. These are fairly representative of the fare structuring in the smaller markets.

On a broader level, potential community benefits from the availability of scheduled air service falls into two categories: Increases in employment and earnings within the local area that result from the airlines's expenditures and the more elusive economic development benefits induced by the presence of scheduled air service.

Employment and earnings benefits are apt to be quite small in non-hub communities. A DOT study of the regional impact of essential air service found that economic development benefits, including the often-cited claims of benefits accruing from the increased attractiveness to businesses of a community receiving scheduled air service, are extremely difficult to quantify.

Upon closer examination, such development benefit claims appear to be made for airports and general aviation facilities rather than for scheduled air service.

Related to this, airline deregulation should have little, if any, impact on the cost of doing business in a small or rural community. These costs in any locality depend heavily on local economic conditions. And, as noted, air service exercises little influence on such conditions.

Furthermore, the availability of capital and the cost of that capital are general functions of national economic conditions and interest rates as well as the condition of the local industrial and economic base and the state of local and regional financial institutions.

Mr. Chairman, airline deregulation has definitely impacted on small and rural communities. The impact of this revolutionary economic regulatory reform is much the same as that felt in larger communities. But, as could be expected, the degree of change is less pronounced.

Fares have declined but that decline is less pronounced than cuts made at large hubs; service opportunities are available but the variety is less pronounced than that found in larger metropolitan areas. This pattern extends across the board when discussing air service at small and rural communities but, quite frankly, I believe you will find this is reflective of all services provided in these areas.

Air service is not any less accessible or more expensive than other services; in fact, I believe it is a better buy and a better service than most others supplied to our rural communities. The benefits of aviation deregulation are being felt in every corner of the country, small as well as larger corners.

That concludes my statement.

[The prepared statement of Mr. Scocozza follows:]

TESTIMONY OF
MATTHEW V. SCOCOZZA
ASSISTANT SECRETARY FOR POLICY AND INTERNATIONAL AFFAIRS
U.S. DEPARTMENT OF TRANSPORTATION
BEFORE THE
SUBCOMMITTEE ON THE RURAL ECONOMY AND FAMILY FARM
OF THE
SENATE COMMITTEE ON SMALL BUSINESS
OCTOBER 28, 1987

MR. CHAIRMAN, MEMBERS OF THE SUBCOMMITTEE, I APPRECIATE HAVING THE OPPORTUNITY TO APPEAR TODAY AS YOU STUDY THE EFFECT OF AIRLINE DEREGULATION ON RURAL COMMUNITIES. THIS CERTAINLY IS A CRITICAL CONSIDERATION IN ANY EVALUATION OF THIS ECONOMIC REGULATORY REFORM. HOWEVER, SINCE THE AVIATION INDUSTRY IS MADE UP OF A COMPLEX SYSTEM OF INTERRELATIONSHIPS, I PROPOSE WE BEGIN WITH A QUICK LOOK AT THE BIG PICTURE.

AS YOU KNOW, AVIATION OPERATIONS WERE DEREGULATED IN 1978 AND THE CHANGES BROUGHT BY THIS POLICY SHAPE TODAY'S MARKET. THE RESULTS? NINE YEARS AGO APPROXIMATELY 39 COMMERCIAL CARRIERS WERE OPERATING. A RECENT COUNT ESTIMATES THAT 131 ARE NOW IN SERVICE. I AM SURE YOU ARE FAMILIAR WITH THE STUDY CONDUCTED BY THE BROOKINGS INSTITUTION WHICH CONCLUDED THAT TODAY AIRLINE TRAVELERS IN THE UNITED STATES ARE ENJOYING $6 BILLION PER YEAR IN 1977 DOLLARS IN LOWER FARES AND MORE FREQUENT FLIGHTS. SINCE 1978, THE NUMBER OF PASSENGER ENPLANEMENTS HAS GROWN BY OVER 140 MILLION -- A 55 PERCENT INCREASE. FURTHERMORE, AN ARTICLE IN <u>DUN'S BUSINESS MONTHLY</u> NOTES THAT THE ECONOMY HAS PROSPERED DUE TO THE REFORMS OF DEREGULATION. "IN AVIATION ALONE," THE ARTICLE SAYS, "DEREGULATION HAS INCREASED THE NATION'S GROSS NATIONAL

PRODUCT BY $8 BILLION IN 1977 DOLLARS...THAT EQUALS A PERMANENT 0.4 PERCENT INCREASE IN GNP."

LET'S CONSIDER A FEW OTHER KEY DEVELOPMENTS IN THE INDUSTRY SINCE ENACTMENT OF THE AIRLINE DEREGULATION ACT:

- SCHEDULED REVENUE PASSENGER MILES INCREASED 61.5 PERCENT, FROM 226 BILLION IN 1978 TO 366 BILLION LAST YEAR; AVAILABLE SEAT MILES INCREASED 64.6 PERCENT, FROM 368 BILLION NINE YEARS AGO TO 606.8 BILLION IN 1986; FREIGHT AND EXPRESS TON MILES ROSE 26 PERCENT, FROM 5.4 BILLION TO 7.3 BILLION.

- THE INDUSTRY WORK FORCE TOTALED 340,483 IN 1978; THAT NUMBER STOOD AT 449,789 LAST YEAR.

MOST IMPORTANT, MR. CHAIRMAN, COMPETITION HAS BEEN ENLIVENED BY DEREGULATION. IN FACT, INDUSTRY COMPETITION IS MORE DYNAMIC AND DIVERSE IN ITS MANY ELEMENTS TODAY THAN EVER BEFORE. CHANGING OPERATING PRACTICES AND MARKETING STRATEGIES ARE WORKING TO RESHAPE THE STRUCTURE AND BUSINESS PRACTICES OF THE AIRLINE SECTOR RESULTING IN THE GREATER COMPETITION WHICH BENEFITS THE CONSUMER, ALL CONSUMERS...RURAL AND URBAN ALIKE.

THE PRESS OF COMPETITION HAS PROMPTED THE AIRLINES TO ALTER SERVICE PATTERNS TO MEET CONSUMER NEEDS. DELIVERING WHAT THE CONSUMER WANTS--INCLUDING ON-LINE SERVICES--HAS LED TO THE DEVELOPMENT OF BUSINESS AFFILIATIONS BETWEEN MAJOR AND REGIONAL CARRIERS, AND THIS PHENOMENON IS RESHAPING SMALL COMMUNITY AIR SERVICE. TODAY, 45 OF THE 50 LARGEST REGIONAL AIR PASSENGER CARRIERS--WHICH COLLECTIVELY FLY MORE THAN 80 PERCENT OF THOSE CARRIED BY REGIONAL OPERATORS--HAVE ENTERED INTO MARKETING ALLIANCES WITH ONE OR MORE LARGE JET OPERATORS.

ALLIANCES BETWEEN MAJOR AND REGIONAL CARRIERS CAN PROVIDE THE RURAL AREA WITH SUBSTANTIAL BENEFITS, INCLUDING INTEGRATION OF SCHEDULES, COOPERATIVE MARKETING AND PROMOTIONAL ARRANGEMENTS, PARTICIPATION BY THE REGIONALS IN THE MAJORS' FREQUENT FLYER PROGRAMS, AND ADDITIONAL ADMINISTRATIVE AND SUPPORT SERVICES. A NUMBER OF MAJOR CARRIERS EVEN PROVIDE THEIR REGIONAL PARTNERS WITH FINANCIAL ASSISTANCE. AMERICAN AIRLINES, FOR EXAMPLE, HAS A $100,000,000 AIRCRAFT LEASING PROGRAM FOR REGIONAL CARRIERS AND EXTENDED $27,000,000, TO AN AMERICAN EAGLE COMMUTER EARLIER THIS YEAR.

AS IS THE CASE IN THE MORE HEAVILY TRAVELED MARKETS, COMPETITION IN THE SMALLER MARKETS IS LIVELY. THOSE REGIONALS AFFILIATED WITH DIFFERENT MAJORS CAN AND DO COMPETE DIRECTLY WITH EACH OTHER IN VARIOUS AREAS; AND REGIONALS OFTEN COMPETE INDIRECTLY WITH ONE ANOTHER BY SERVING ALTERNATIVE HUB AIRPORTS, THUS PROVIDING TRAVELERS WITH MORE PRICE AND SERVICE OPTIONS.

RELATED TO THIS, IN 1978 NOT EVERY STATE HAD REGIONAL/COMMUTER SERVICE; TODAY THERE ARE REGIONAL/COMMUTER AIR CARRIERS OPERATING IN EACH STATE. AS REVEALED IN A RECENT DEPARTMENT OF TRANSPORTATION STUDY 1/ MOST STATES HAVE EXPERIENCED AN INCREASE IN THE NUMBER OF REGIONAL/COMMUTER CARRIERS OPERATING WITHIN THEM. IN ADDITION, THE INDUSTRY FLEET HAS GROWN SUBSTANTIALLY SINCE 1978, BOTH IN OVERALL NUMBER AND IN VARIETY OF SIZES AND TYPES OF EQUIPMENT. ALTHOUGH COMMUNITIES HAD BECOME ACCUSTOMED TO SERVICE WITH LARGER AIRCRAFT, THEIR TRAFFIC LEVELS OFTEN DID NOT WARRANT THOSE LEVELS OF AVAILABLE CAPACITY. MANY WERE BEING OVER SUPPLIED. WITH DEREGULATION A MORE RATIONAL MATCHING OF EQUIPMENT WITH MARKET SIZE WAS INEVITABLE. INITIALLY, MANY COMMUNITIES DID NOT RESPOND FAVORABLY WHEN 50 TO 100-SEAT AIRCRAFT OPERATIONS WERE REPLACED WITH 15 TO 50-SEAT OR SMALLER COMMUTER AIR CARRIER SERVICE. BY NOW, HOWEVER, THE EQUIPMENT RESTRUCTURING IS LARGELY COMPLETE AND, WITH FEW EXCEPTIONS, THE AIRCRAFT BEING USED REASONABLY MATCH THE LEVEL OF DEMAND. TODAY, 17-19 SEAT SWEARINGEN METROLINERS, 19-SEAT BEECH 1900'S, 30-36 SEAT SHORTS AND 50-SEAT DASH 7 AIRCRAFT ARE WIDELY USED IN THE INDUSTRY. EQUALLY IMPORTANT, A WIDE VARIETY OF SIZES OF AIRCRAFT IS BEING OPERATED IN EVERY REGION OF THE COUNTRY, ENABLING REGIONAL/ COMMUTERS TO MEET ALL LEVELS OF MARKET DEMAND.

1/ Report to Congress on Subsidized Air Service Under the Essential Air Service Program -- Section 419 of the Federal Aviation Act, U.S. Department of Transportation, Washington, D.C., February 1987.

MR. CHAIRMAN, THE GENERAL ECONOMIC IMPACT OF AIRLINE DEREGULATION ON SMALL AND RURAL COMMUNITIES CANNOT BE VIEWED SEPARATE AND APART FROM THE GENERAL ECONOMIC CONDITIONS OF A PARTICULAR AREA. THIS IS ESPECIALLY TRUE WHEN STUDYING THE HEALTH OF AREAS DOMINATED BY AGRICULTURE AND RELATED INDUSTRIES.

AS WE CONSIDER THE SUBJECT BEFORE US TODAY, LET'S KEEP IN MIND THAT WHEN CONGRESS ENACTED THE AIRLINE DEREGULATION ACT, IT ALSO ACTED TO PRESERVE AIR SERVICE TO SMALL COMMUNITIES. THE SOLE PURPOSE OF THE ESSENTIAL AIR SERVICE PROGRAM WAS, AND IS, TO GUARANTEE CONTINUED ACCESS TO THE AIR TRANSPORTATION SYSTEM BY SMALL AND ISOLATED POINTS WHICH HAD BEEN A PART OF THE AIR TRANSPORT NETWORK PRIOR TO DEREGULATION. THIS PROGRAM GUARANTEES THAT SMALL COMMUNITIES WHICH HAD AIRLINE SERVICE BEFORE DEREGULATION WOULD CONTINUE TO BE SERVED BY AN AIR CARRIER FOR TEN YEARS, UNTIL OCTOBER 1988. FOR COMMUNITIES IN THE EAS PROGRAM, NO AIR CARRIER MAY TERMINATE OR REDUCE SERVICE IN A MANNER THAT WILL LOWER THE COMMUNITY'S TOTAL SERVICE BELOW THE GUARANTEED LEVEL WITHOUT FILING NOTICE WITH THE DEPARTMENT OF TRANSPORTATION, AS WELL AS THE APPROPRIATE STATE AGENCIES AND COMMUNITIES INVOLVED. IN THE CONTIGUOUS 48 STATES, 468 POINTS WERE PROTECTED UNDER THE ESSENTIAL AIR SERVICE PROGRAM IN 1978. THE EAS PROGRAM WAS SUCCESSFUL IN STABILIZING SERVICE TO RURAL AND SMALL COMMUNITIES. AS YOU KNOW, WE AT THE DEPARTMENT ARE ADVOCATING THE SUNSET OF THIS PROGRAM AFTER A JOB WELL DONE.

THERE IS NO DENYING THE FACT, MR. CHAIRMAN, THAT MANY OF THOSE COMMUNITIES NOT INCLUDED UNDER THE EAS PROTECTIVE BLANKET LOST

SERVICE. HOWEVER, THE IMPACT OF THESE REDUCTIONS WAS OFTEN CUSHIONED BY THE AVAILABILITY OF SERVICE AT NEARBY AIRPORTS. A RECENT STUDY BY PATRICK V. MURPHY AND WAYNE S. WATKINS 2/ CONDUCTED A RANDOM SAMPLING OF VARIOUS POINTS THAT LOST SERVICE AND DISCOVERED THAT ALL ARE WITHIN 21 TO 128 MILES OF AN ALTERNATE AIRPORT.

IT SHOULD ALSO BE NOTED HERE TODAY THAT INDUSTRY COMPETITION SPURRED BY DEREGULATION HAS PROMPTED A DECLINE IN FARES TO MARKETS OF ALL SIZES. (SEE TABLE 1) WHILE THE DECLINE IN REAL FARES HAS BEEN MORE PRONOUNCED IN MAJOR MARKETS, SUCH AS LARGE HUB-TO-LARGE HUB ROUTES--WHERE FARES HAVE DECLINED BY 17 PERCENT ON AVERAGE--EVEN IN THE SMALLEST MARKETS, FARES HAVE DECLINED AN AVERAGE OF SEVEN PERCENT.

IN THE MAJOR MARKETS, LOW-COST CARRIERS INAUGURATED SERVICE AT FARES BELOW NORMAL COACH FARES. THEIR FARES IN TURN FORCED THE HAND OF COMPETING CARRIERS. FURTHER, THE NUMBER AND DEPTH OF DISCOUNT FARES INCREASED GREATLY IN DIRECT PROPORTION TO THE SIZE OF THE MARKET SERVED. CONSEQUENTLY, LARGE MARKETS HAVE A WIDER RANGE OF DISCOUNT FARES THAN DO SMALL MARKETS.

THE MORE MODEST FARE REDUCTIONS IN SMALLER MARKETS ARE NOT SURPRISING. TRADITIONALLY, LOW DENSITY MARKETS HAVE HAD FEWER FARE AND SERVICE OPTIONS AVAILABLE. WITH A SMALLER BASE OF

2/ Murphy, Patrick V. and Watkins, Wayne S., "Rural America Benefits from Airline Deregulation, but Less than Urban America," Rural Development Perspective, October 1986, pages 2-7. Both authors were DOT employees when this article was written.

CONSUMERS, IT STANDS TO REASON THAT OPERATING COSTS WOULD BE HIGHER, SERVICE LESS FREQUENT, AND THE FARE STRUCTURE TIGHTER. TODAY'S MARKET SIMPLY REFLECTS ECONOMIC REALITY.

ALSO, SOME OF THE DIFFERENCES IN FARE CHANGES IS DUE TO THE ELIMINATION OF CROSS-SUBSIDY AMONG DIFFERENT CATEGORIES OF PASSENGERS. BEFORE DEREGULATION, CARRIERS TENDED TO OVERPRICE IN HEAVILY TRAVELED LONG-HAUL MARKETS AND UNDERPRICE IN LIGHTLY TRAVELED MARKETS. THIS POLICY WAS THE DIRECT RESULT OF CIVIL AERONAUTICS BOARD FARE FORMULAS DESIGNED TO ENCOURAGE GROWTH IN SHORT-HAUL AND LIGHTLY TRAVELED MARKETS.

WHATEVER THE DISPARITY FOUND BETWEEN FARE STRUCTURES OF LARGE AND SMALL MARKETS, THE DIFFERENCES CAN BE JUSTIFIED BY COST ANALYSES. THE DEPARTMENT OF TRANSPORTATION STUDY REFERRED TO EARLIER ANALYZES THE COST OF PROVIDING SERVICE TO SMALLER MARKETS, AND UPON COMPARING THE COSTS WITH ACTUAL FARES CHARGED IN VARIOUS MARKETS, IT WAS DISCOVERED THAT THE CURRENT PRICING POLICIES OF COMMUTER CARRIERS ARE QUITE REASONABLE. (SEE TABLES 2 AND 3.) FOR EXAMPLE, IN A 125-MILE MARKET WITH 5 ENPLANEMENTS PER DAY, THE ECONOMIC COST PER PASSENGER RANGES FROM A LOW OF $139.45 FOR AN EIGHT-SEAT AIRCRAFT, TO $322.47 FOR A 44-SEAT, F-27 AIRCRAFT. THUS, IN ORDER FOR A 125-MILE MARKET WITH FIVE ENPLANEMENTS PER DAY TO SUPPORT AIR SERVICE ON ITS OWN--WITHOUT FEDERAL SUBSIDY--THE ONE-WAY FARE WOULD HAVE TO BE WELL OVER $100. COMPARING THIS FIGURE WITH VARIOUS FARES CHARGED IN ESSENTIAL AIR SERVICE MARKETS WE FIND SKY WEST CHARGING $126 IN THE PAGE-PHOENIX CONNECTION, A

DISTANCE OF 242 AIR MILES WITH 13 ENPLANEMENTS PER DAY. SIMILARLY, IN THE LAMAR-DENVER MARKET, A DISTANCE OF 166 MILES WITH FOUR ENPLANEMENTS PER DAY, AIR MIDWEST IS CHARGING $119. THESE ARE FAIRLY REPRESENTATIVE OF THE FARE STRUCTURES FOUND IN THE SMALLER MARKETS.

ON A BROADER LEVEL, POTENTIAL COMMUNITY BENEFITS FROM THE AVAILABILITY OF SCHEDULED AIR SERVICE FALL INTO TWO CATEGORIES: INCREASES IN EMPLOYMENT AND EARNINGS WITHIN THE LOCAL AREA THAT RESULT FROM THE AIRLINE'S EXPENDITURES, AND THE MORE ELUSIVE ECONOMIC DEVELOPMENT BENEFITS INDUCED BY THE PRESENCE OF SCHEDULED AIR SERVICE. EMPLOYMENT AND EARNINGS BENEFITS ARE APT TO BE QUITE SMALL IN NON-HUB COMMUNITIES. A DOT STUDY OF THE REGIONAL IMPACT OF ESSENTIAL AIR SERVICE 3/ FOUND THAT ECONOMIC DEVELOPMENT BENEFITS, INCLUDING THE OFTEN-CITED CLAIMS OF BENEFITS ACCRUING FROM THE INCREASED ATTRACTIVENESS TO BUSINESSES OF A COMMUNITY RECEIVING SCHEDULED AIR SERVICE, ARE EXTREMELY DIFFICULT TO QUANTIFY. UPON CLOSER EXAMINATION, SUCH DEVELOPMENT BENEFIT CLAIMS APPEAR TO BE MADE FOR AIRPORTS AND GENERAL AVIATION FACILITIES RATHER THAN FOR SCHEDULED AIR SERVICE.

SOME LIMITED EVIDENCE SUGGESTS THAT AIRPORTS AND THE TYPE OF SERVICES THEY PROVIDE MAY WELL BE CONSIDERATIONS FOR THE SITING OF CERTAIN TYPES OF BUSINESS AND INDUSTRIAL FACILITIES, BUT THERE IS NO EVIDENCE THAT THE EXISTENCE OF SCHEDULED SERVICE AT THESE

3/ Essential Air Service: Regional Impacts, U.S. Department of Transportation, Research and Special Programs Administration, Transportation System Center, Cambridge, Mass., December 1986.

AIRPORTS HAS COMPARABLE EFFECTS ON LOCATION DECISIONS. EVEN IN CASES WHERE AIRPORTS AND SERVICES ARE SITING CONSIDERATIONS, THE DESIRABILITY OF AN AIRPORT MAY PLACE WELL DOWN ON A LIST OF SELECTION FACTORS, BELOW ITEMS SUCH AS PROXIMITY TO IMPORTANT MARKETS, AVAILABILITY OF RAW MATERIALS, LABOR, UTILITIES, TAX TREATMENT, AMENITIES, AND SITE SUITABILITY.

A 1970 STUDY BY LEONARD F. WHEAT FOUND THAT FOR CITIES IN THE NORTHEAST BELOW 19,000 POPULATION THERE WAS NO EVIDENCE THAT THE PRESENCE OF AIR SERVICE HAD AN IMPACT UPON MANUFACTURING EMPLOYMENT GROWTH. FOR LARGER CITIES, HE CONCLUDED THAT AIR SERVICE PROBABLY PROMOTED GROWTH, BUT FOUND THE BENEFITS TO BE "SEVERELY LIMITED."4/

A 1975 NASA-FUNDED STUDY OF GENERAL AVIATION IMPACTS CONCLUDED THAT UNLESS OTHER FREQUENTLY MENTIONED FACTORS WERE PRESENT, IT WAS UNLIKELY THAT THE LACK OF AVIATION SERVICES WOULD DETER AN OTHERWISE INTERESTED COMPANY.5/

A STUDY OF RESPONSES TO A NEBRASKA SURVEY OF INDUSTRIAL PLANTS FOUND THAT AIR PASSENGER TRANSPORTATION RATED 36TH IN IMPORTANCE OUT OF 43 POSSIBLE FACTORS.6/ A 1975 STUDY BY THE MINNESOTA

4/ Wheat, Leonard F., The Effect of Airline Service on Manufacturing Growth in Cities Below 40,000 Population, Economic Development Administration, U.S. Department of Commerce, May 1970.

5/ Dayani, J., and Sinoff, M., General Aviation and Community Development, NASA Langley Research Center and Old Dominion University, Norfolk, VA, 1975.

6/ Whiting, Larry R., Rural Industrialization: Problems and Potentials, Iowa State University Press, Ames, Iowa, 1974.

DEPARTMENT OF AERONAUTICS FOUND AIR SERVICE ACCESSIBILITY IN THE BOTTOM HALF OF LOCATIONAL CONSIDERATIONS LISTED FOR ALL TYPES OF INDUSTRIES AND COMMUNITIES STUDIED.7/

IN SUMMARY, A SURVEY OF THE LITERATURE INDICATES THAT THE VARIOUS BUSINESSES STUDIED TO DETERMINE THE IMPORTANCE OF AVIATION SERVICES APPEARED TO BE PRIMARILY CONCERNED WITH ACCESS TO A GENERAL AVIATION AIRPORT, AND THE PRESENCE OF A FIXED BASE OPERATOR TO SUPPORT PRIVATE BUSINESS AIRCRAFT AND AIR-TAXI SERVICE. THE AVAILABILITY OF SCHEDULED AIR SERVICE WAS NOT HIGHLY RATED NOR, IN MOST CASES, EVEN EXPRESSED AS A FACTOR INFLUENCING BUSINESS LOCATION DECISIONS.

RELATED TO THIS, AIRLINE DEREGULATION SHOULD HAVE LITTLE, IF ANY, IMPACT ON THE COST OF DOING BUSINESS IN A SMALL OR RURAL COMMUNITY. THESE COSTS IN ANY LOCALITY DEPEND HEAVILY ON LOCAL ECONOMIC CONDITIONS. AND, AS NOTED, AIR SERVICE EXERCISES LITTLE INFLUENCE ON SUCH CONDITIONS.

FURTHERMORE, THE AVAILABILITY OF CAPITAL AND THE COST OF THAT CAPITAL ARE GENERAL FUNCTIONS OF NATIONAL ECONOMIC CONDITIONS AND INTEREST RATES AS WELL AS THE CONDITION OF THE LOCAL INDUSTRIAL/ ECONOMIC BASE AND THE STATE OF LOCAL AND REGIONAL FINANCIAL INSTITUTIONS.

7/ A Study of the Socio-Economic Impact of Aviation on Selected Communities, Minnesota Department of Aeronautics, January 1975.

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MR. CHAIRMAN, AIRLINE DEREGULATION HAS DEFINITELY IMPACTED ON SMALL AND RURAL COMMUNITIES. THE IMPACT OF THIS REVOLUTIONARY ECONOMIC REGULATORY REFORM IS MUCH THE SAME AS THAT FELT IN LARGER COMMUNITIES, BUT--AS COULD BE EXPECTED--THE DEGREE OF CHANGE IS LESS PRONOUNCED. FARES HAVE DECLINED BUT THAT DECLINE IS LESS PRONOUNCED THAN CUTS MADE AT LARGE HUBS; SERVICE OPPORTUNITIES ARE AVAILABLE BUT THE VARIETY IS LESS PRONOUNCED THAN THAT FOUND IN LARGER METROPOLITAN AREAS. THIS PATTERN EXTENDS ACROSS THE BOARD WHEN DISCUSSING AIR SERVICE AT SMALL AND RURAL COMMUNITIES BUT, QUITE FRANKLY, I BELIEVE YOU WILL FIND THIS IS REFLECTIVE OF ALL SERVICES PROVIDED IN THESE AREAS. AIR SERVICE IS NOT ANY LESS ACCESSIBLE OR MORE EXPENSIVE THAN OTHER SERVICES; IN FACT, I BELIEVE IT IS A BETTER BUY AND A BETTER SERVICE THAN MOST OTHERS SUPPLIED TO OUR RURAL COMMUNITIES. THE BENEFITS OF AVIATION DEREGULATION ARE BEING FELT IN EVERY CORNER OF THE COUNTRY, SMALL AS WELL AS LARGER CORNERS.

THAT CONCLUDES MY FORMAL STATEMENT.

Table 1

Prices in Airline Markets, by Type, 1979 and 1985

Market Type	Real Price (Cents per Mile)* 1979	1985
Large Hub-Large Hub	4.4	3.6
Large Hub-Medium Hub	4.7	4.0
Large Hub-Small Hub	4.9	4.1
Large Hub-Nonhub	5.3	4.6
Medium Hub-Medium Hub	4.9	4.1
Medium Hub-Small Hub	5.1	4.4
Medium Hub-Nonhub	5.5	5.1
Small Hub-Small Hub	5.4	4.8
Small Hub-Nonhub	5.7	5.3
Nonhub-Nonhub	6.2	5.8

* Real price is total real revenues divided by total revenue passenger miles flown. It is used here in lieu of actual dollar fares to correct for differences in trip length between the two periods.

Table 2

COMPARATIVE COST ANALYSIS
125 MILES

	Piper T-1020	Beech C-99	Metro IIIA	Shorts 360	F-27
Direct Expense 1/	$238,476	$313,286	$357,300	$495,876	$651,300
Indirect Expense 2/	178,857	219,300	250,110	322,319	423,345
Total Operating Expense	$417,333	$532,586	$607,410	$818,195	$1,074,645

1/ Assumes the following annual block hours and costs per hour:

Flying Operations	$ 75	$ 90	$ 95	$120	$130
Fuel & Oil	53	66	72	96	130
Maintenance	70	90	120	140	220
Depr. & Interest/Rentals	40	80	110	160	100
Total Directs	$238	$326	$397	$516	$650
Block Hours	1,002	961	900	961	1,002

2/ Assumes the following percentages, indirects of directs:

	75%	70%	70%	65%	65%

Table 3

TOTAL ECONOMIC COST PER PASENGER FOR VARYING
ANNUAL PASSENGER AMOUNTS BY STAGELENGTH BY AIRCRAFT TYPE

Aircraft Type/Milage	Total Economic Cost Per Passenger For Varying Annual Passenger Amounts			
	3,130 (5/day)	6,260 (10/day)	9,390 (15/day)	12,520 (20/day)
Piper T-1020				
75	$112.30	$ 74.30	$ 61.47	$ 55.00
125	139.45	94.39	79.07	71.25
200	177.85	123.06	104.46	95.00
300	229.21	162.34	139.44	127.67
Beech C-99				
75	$134.57	$ 69.57	$ 47.91	$ 47.57
125	171.06	88.34	60.77	60.86
200	224.56	115.88	79.65	81.48
300	291.15	150.23	103.25	108.30
Metro III A				
75	$146.92	$ 75.75	$ 52.02	$ 40.16
125	192.63	99.13	67.96	52.38
200	250.41	128.81	88.27	68.00
300	318.80	164.05	112.47	86.67
Shorts 360				
75	$191.13	$ 97.86	$ 66.76	$ 51.22
125	244.38	125.00	85.21	65.31
200	326.55	166.88	113.65	87.04
300	429.50	219.40	149.37	114.35
F-27				
75	$262.20	$133.38	$ 90.45	$ 68.98
125	322.47	164.05	111.24	84.84
200	417.22	212.21	143.87	109.70
300	533.75	271.52	184.12	140.41

The CHAIRMAN. Thank you.
Mr. Cadwell.

STATEMENT OF CHARLES A. CADWELL, DEPUTY CHIEF COUNSEL FOR ADVOCACY, U.S. SMALL BUSINESS ADMINISTRATION, WASHINGTON, DC

Mr. CADWELL. Thank you, Mr. Chairman. I want to convey Senator Abdnor's regrets, as he is just getting back into town today. As you well know, this is an issue of long concern to the Administrator from his service as representing the State of South Dakota.

I appreciate the opportunity to join you this morning, and I think after your hearing, there can be no doubt that the quality and level of air service is an important concern for those who are concerned about rural and economic development.

Since Frank Swain appeared before this Subcommittee in March, the first of your several hearings, we at SBA have taken several steps to increase our activities in the area of rural development. I wanted to report on those, but also note at the outset that we do not have the specific sorts of information or resource that the Department of Transportation has on the specific impact of airline service increases and decreases to rural areas.

We do, I think, bring a perspective on rural development that recognizes the value of air service for rural communities. The small business jobs miracle that has been so important to our overall economic growth in this country has largely been an urban phenomenon.

In rural areas, small firms with fewer than 500 employees have increased their employment only about 23 percent. In urban areas, those same small firms have increased their employment 30 percent in the period between 1976 and 1984. That means in rural areas small business is growing about one-third more slowly than in urban areas. There are a lot of factors that account for that, but it is either a cause and effect or a little bit of both I suspect.

It seems to me that policies to expand jobs and to expand economic development in rural areas needs to focus on small business development. In rural areas, this challenge is going to be increased significantly in the coming years as our workforce grows more slowly, as migration patterns from rural to urban America continue, and particularly where the rural workforce apparently, according to Labor Department studies, is already somewhat less educated, has lower educational levels than the urban workforce.

This creates problems for rural communities seeking to expand into the new service industries, high-tech industries that are even greater than they are in urban areas.

As you know, of course, there are several components to an economic development policy. To reach these problems, we need to be concerned about economic policy affecting interest rates and basic commodity prices.

The CHAIRMAN. Would you please focus on air service, to save time.

Mr. CADWELL. OK. I will say this with respect to air service. I recently had the opportunity to meet with many State legislators, local government officials, on the issue of rural development. The

issues of infrastructure, air service, roads, educational systems, are all very important issues to them. I think that there are two observations that I would make based on those meetings with those people.

One was that there seems to be wide recognition that there is not a broad pool of new resources to devote to solving these problems in terms of Federal or State revenues and money.

Second, is that one of the key concerns that they have is that we at the Federal level do not coordinate our existing assistance very well, and that particularly at the local level Federal officials do not always work well together or do not work in response to local leaders. We are not a demand-driven Federal Government.

So, there are three things that we are doing at SBA that Senator Abdnor is undertaking to address these issues. One is that we are measuring the extent of our assistance to rural areas. That is something that we have not been able to do in the past, and are commencing in part at the instance of your March hearing.

Second, the Senator will announce today or tomorrow, a series of five hearings across the country to listen to rural problems. Third, following those hearings, we hope to establish a series of 10 meetings to bring together a network of Federal, State, local and small business leaders to actually look at local problems, local solutions, so that we can best provide service.

With respect to airline service specifically, as I indicated to your staff, we do not have specific information. It is not an issue that until listening to your excellent witnesses this morning, we have heard a lot about at the SBA. That is not to say that it is not an issue, but it is not one that we have heard about previously.

[The prepared statement of Mr. Cadwell follows:]

U.S. SMALL BUSINESS ADMINISTRATION
WASHINGTON, D.C. 20416

OFFICE OF CHIEF COUNSEL FOR ADVOCACY

Statement of

Charles A. Cadwell

Deputy Chief Counsel for Advocacy

U.S. Small Business Administration

Before The

Senate Small Business Committee

Subcommittee on the Rural Economy and Family Farming

October 28, 1987

Mr. Chairman I appreciate the opportunity to participate in today's hearing, as part of a series on rural development issues that you have conducted. Since Frank Swain appeared here in March, we at the Small Business Administration have taken several steps to increase our activities in the area of rural development. I should note at the outset, that on the specific issue of today's hearing, the impact of airline deregulation, we do not have specific information such as has been collected by researchers at the Department of Transportation. We do bring nonetheless, a perspective on rural development that recognizes the value of air service to a rural community.

The small business jobs miracle that we have experienced here in the United States is largely an urban phenomenon. In rural areas small firms are not contributing new jobs at the same rate as in urban areas. Some specifics: between 1976 and 1984 the number of jobs in firms with fewer than 500 employees grew 31% in urban areas and only 23% in rural areas. In other words, small business job growth is about 30% slower in rural areas than it is in urban areas. Furthermore, we're finding that the growth that does occur in rural areas is receiving a greater boost from large firms, primarily in the health services and education services areas.

There are many possible explanations for the different rates of small business job growth. It may well be that the employment activity is simply a mirror of population shifts, reflecting the net population outflow from rural areas. Other reasons for the slower growth in small business jobs may be that the market specificity which small business thrives on is easier to create in large urban markets or it may be that rural areas are exporting their youth, their people with ideas and their entrepreneurs.

In any event the policies to create jobs in rural areas, to broaden the American jobs miracle from our urban areas to include rural America, need to be, it seems to me, policies that promote the formation and the expansion of small business. This challenge in rural areas is intensified by some of the demographics changes that we expect will affect the entire economy over the next 15 years. First among those is the slowing of the population growth. From a population that grew at almost 2% in the 1950's, by the year 2000 our population and our work force will be growing at less than 1% per year. This has some very important impacts on job creation and on the social burden on governments and on employers. It means that there will be more older workers, it means that there will be essentially no growth in the number of entry level workers. If people are leaving a community anyway, the challenge to employers, to our educational system and to economic development is multiplied dramatically. Apparently studies show that the rural work force is already less trained and less educated than the urban work force. Employers seeking to find workers in rural areas thus are going to have a even harder time.

The components of a climate conducive to small business formation and growth are both macro-economic and policy specific. They include:

- Interest rates, the rate of inflation
- Worldwide commodity prices (both agricultural and energy)
- Federal, state and local regulatory climates
- Workforce regulations
- Local infrastructure
  - Roads, airports, sewers
  - Education system
  - Financial service institutions

In meetings with dozens of local officials, state legislators and small business owners, I have found wide recognition that we cannot expect to find new Federal or state resources to solve rural problems. Instead, local leaders are asking that those of us at the Federal level do a much better job of coordinating our existing assistance and that we do a better job of disseminating information about existing programs.

In every example of successful rural development, the common thread is strong local leadership to which state and Federal agencies respond. The key is not generally a mandate from Washington that says something like, "Every SBA office shall give two more loans to rural areas." Our job is to insure that at the local level state and federal policymakers work together and that they work in response to local needs. This occurs in many areas, unfortunately it is my experience that it does not occur as often as it must. At a meeting of rural state legislators recently, this was the single greatest request directed at those of us on the Federal level, not new, grand programs, or new policy or regulatory schemes.

Let me review briefly what is occurring at SBA.

Under the direction of Administrator Abdnor we are:

- Measuring current levels of service to rural areas.
- Listening to rural problems.
- Establishing networks for local initiative.

Your attention to air service, as one important component of a healthy climate for small business is welcome Mr. Chairman and we look forward to working with you as you move ahead in your series of hearings.

The CHAIRMAN. Thank you. I think for the sake of time, I will ask the other witnesses to come up too, and I will ask questions of all four of you.

We have John Fredericksen, Regional Airline Association, executive vice president; and Mr. James Landry, senior vice president and general counsel, Air Transport Association of America.

Mr. Fredericksen, why do you not give your testimony and then Mr. Landry, and then I will ask questions of all four of you.

STATEMENT OF JOHN S. FREDERICKSEN, EXECUTIVE VICE PRESIDENT, REGIONAL AIRLINE ASSOCIATION, WASHINGTON, DC

Mr. FREDERICKSEN. Thank you, Mr. Chairman.

There are a couple of matters that have come up, I think, while I have been sitting here in the hearing room today that I think I should point out from our point of view.

One is that it is no secret, Mr. Chairman, that my segment of the industry that I represent, that is the propeller industry, has grown dramatically since deregulation. The reason that it has grown is very simple; it is that many communities in this country simply could not afford jet service, it was not economical. Therefore, you see the progression toward propeller airplanes.

It does not take an economics major to figure that out, Mr. Chairman. When I talked to my members basically who are, like I say, the propeller operators of the country, there is not a single one of them who would not like to operate bigger airplanes. The bottom line is you can make more money with a bigger airplane if you can fill it up with people.

I talked to Terry Marshall, who runs Big Sky out in Montana. He would love to operate Saab 340s, which is one of the airplanes that was mentioned here earlier today. It is a state-of-the-art, $6 million, 36-seat airplane. Terry Marshall would love to operate Saab 340s at Big Sky. The fact is, he simply does not have the traffic out there to support this airplane.

There is another issue that has come up repeatedly here today, Mr. Chairman, and that is an issue that those of us in the regional airline industry just cannot afford to sit by and ignore. When people make statements on the record that deregulation has had a deleterious effect on safety, it seems to become a common perception, certainly in this hearing room this morning. That is absolute boloney, and I would be more than happy to send you the figures to show that since deregulation came into effect, the safety record for the commuter industry has improved almost six times.

The CHAIRMAN. I am sorry, Mr. Fredericksen. We have a very unfortunate coincidence in timing here. The EAS amendment is at this moment, on the floor. I am afraid that I am going to have to temporarily recess this hearing. I will speak as briefly and succinctly as I possibly can and return right away.

So, I have to ask the indulgence of all the witnesses. My guess is that I'll be away for about 10 or 15 minutes.

[A brief recess was taken.]

The CHAIRMAN. Mr. Fredericksen, I apologize for interrupting your speech.

Mr. FREDERICKSEN. No apology necessary, Mr. Chairman, the Essential Air Service Program is very important to us as well, so we are happy to have taken a break for that.

As I was saying, I would be more than happy to provide the Chair with the actual numbers from the National Transportation Safety Board to back up my assertions that under deregulation our segment of the industry has improved its safety record really quite dramatically.

Every year except for one, we have had improvement. On a departure basis now, the commuter industry is really six times safer than it was in 1978. I laid out the reasons for that in my paper there. A lot of it has to do with the increased FAA enforcement, and a lot of it has to do with better economic conditions because of the deregulation our carriers have experienced.

To be brief though, I think you would like to hear what we would like to suggest that you do about some of these problems with reduced air service in rural communities. I think one of the most important things that you can do as a Congress is to resist the capacity controls, artificial capacity controls, at the hub airports. That is really a driving force behind some of this reduced service in the rural areas.

If there is only so many slots that an air carrier has, he is forced to operate those slots into the absolute most lucrative areas. The overall answer is, of course, is to provide a more efficient airport system where we can get more airplanes in through better air traffic or through building more runways. If you see that at the hub airports, you will see the rural airports prospering as well.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Fredericksen follows:]

80-152 - 88 - 7

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STATEMENT OF

JOHN S. FREDERICKSEN

EXECUTIVE VICE PRESIDENT

OF THE

REGIONAL AIRLINE ASSOCIATION

BEFORE THE

SENATE COMMITTEE ON SMALL BUSINESS

SUBCOMMITTEE ON THE RURAL ECONOMY AND FAMILY FARM

Regarding the Effect of Airline Deregulation

on the Rural Economy

October 28, 1987

Washington, D.C.

Thank you, Mr. Chairman, for the opportunity to present the views of the Regional Airline Association regarding the effect of airline deregulation on service to rural America. RAA represents 75 member airlines, the bulk of whom are in the business of moving passengers between this country's smaller communities and the major hub airports using primarily propeller aircraft.

Regional airlines served 784 airports in the U.S. in January 1987, according to RAA surveys. We served 225 of those airports in conjunction with large carriers using jet equipment, and the remaining 559 exclusively with regional aircraft. In June 1979, we served only 603 airports, with exclusively regional service at 459 cities. Clearly, the regional airline industry has expanded to serve many more communities than we did prior to deregulation.

The evolution of the Essential Air Service program paints a similar picture. On January 1987, regional airlines served 309 of the 316 points in the United States (excluding Alaska) eligible for essential air service. Regional carriers served 84% (266) of those points exclusively, while serving jointly with a major or national carrier at 43 additional points. Those figures have changed dramatically since 1978, when regionals served exclusively only 35% of the total number of EAS points. The dominant role in EAS has been assumed by regional carriers.

While regionals have expanded into some markets which received no air service at all prior to deregulation, much of the growth has occurred at those points where jet service is simply not economically feasible. In many markets, frequent jet service has been replaced, because of simple economic necessity, by jet

service only during peak hours, supplemented with regional airline service during off-peak hours.

The profit potential of a large airplane will always exceed that of a smaller airplane, if the market can provide the passengers to fill it. Under deregulation, the marketplace has demonstrated dramatically its ability to adjust airplane size and frequency to the available passenger base. If a community could not support service with a large propeller airplane for example, the company that provided reliable, frequent service with a smaller propeller airplane could still operate. If passengers did not buy tickets for the mid-day or late evening flights, those frequencies were cancelled, and the aircraft put to better use elsewhere.

In those communities qualifying for EAS subsidies, of course, the marketplace was somewhat supplemented by the federal subsidy. Even so, the low level of federal subsidy could rarely sustain frequent service by large aircraft. Even with an EAS subsidy, therefore, the rule that the smaller airplane, when full, will always outlast the half empty large airplane prevails.

Many people believe that the downsizing of aircraft is itself a cause for a reduction in traffic volume at an airport. While there may be some truth to that, I should emphasize again that airlines will tend to operate the largest equipment the market will sustain, since the profit potential for the larger airplane is higher. It is important to keep in mind, however, that many carriers have demonstrated that frequency and reliability were as important as aircraft size in generating

traffic. Certainly, the underlying economy of a community is the primary driving force behind passenger traffic. In the areas where relatively depressed industries such as oil or agriculture have been dominant, a reduction in airline service and a rise in airline bankruptcies, have occurred.

Safety

While the shape of the regional airline industry under deregulation is still far from fully defined, it is clear that safety has not suffered. The accident rates for the Part 135 (30 seats or fewer) scheduled carriers have improved every year except one since 1978. The rate of accidents per 100,000 departures for the Part 135 carriers was almost six times better in 1986 than in 1978. There is statistically almost no difference between the accident rates of the regionals who operate under Part 121 (31 or more seats) and that of the major carriers, who operate under the same rules.

There are several reasons why the safety record of the commuters has improved under deregulation. Economic growth has enabled the carriers to purchase more modern, state of the art equipment. The industry welcomed and encouraged the FAA regulatory initiatives that were instituted at the same time economic regulation was decreased. Certainly the upgrade in Part 135 standards, which took place at the beginning of deregulation, has been effective. So too has the more intense and sophisticated FAA scrutiny of the regionals, as well as the FAA's effort to standardize enforcement practices on a national level.

Airport Capacity

Probably the largest threat to air service in smaller communities is the over-capacity problems being experienced at many of the nation's hub airports. Chicago O'Hare is the classic example because the slot limitations force carriers to use the valuable slots with the largest aircraft possible, thereby automatically putting the smaller communities at a disadvantage. There are continuing initiatives to institute slot controls at additional airports. Fortunately, none of those efforts have so far been successful.

The Massachusetts Port Authority, for example, is preparing to take a step backward by attempting to use discriminatory pricing to exclude commuter aircraft from Boston Logan. The result of such a program, of course, is that small communities in New England will be priced out of their air service. If other operators of hub airports decide, like MassPort, to limit air commerce rather than growing and adjusting to accommodate growth, airline service to many parts of rural America will be severely threatened.

Community Action

No one disputes the importance of scheduled airline service to the economic vitality of a community. Certainly, the airline community is always searching for viable markets and we have shown the ability to respond very quickly to business opportunities. In cases where air carriers have reduced or eliminated service because of losses, however, the community must take a primary role in helping to develop and promote better service.

An excellent example of a successful community program was reported in this month's Airport Services magazine. The citizens of Redmond, Oregon felt that they needed direct air service to San Francisco, even though a carrier had tried and failed in that market. Redmond used corporate pledges to build an escrow account to indemnify an airline if service fell below a set level, and eliminated landing fees. The resulting startup air service has exceeded expected passenger levels, with the result that increased rental car fees have replaced the landing fees, and the escrow fund remains untouched.

Airline service to small communities is the primary reason the regional airlines exist. We will continue to provide the very best service possible to any American market that can sustain profitable operations.

Reregulation is Not the Answer

We urge the Congress to aid us in that endeavor by ensuring that artificial constraints at the nation's hub airports are not permitted to discriminate against the citizens of rural areas. We also urge the Congress to recognize that new non-safety related regulation like the consumer protection bills now pending, if applied to all airlines regardless of size, will only increase the expense of small community air service, and, thus, the price of a ticket. Those added expenses can mean the difference between air service and no air service in those markets where profitability is already marginal.

The CHAIRMAN. Thank you. Mr. Landry.

STATEMENT OF JAMES E. LANDRY, SENIOR VICE PRESIDENT AND GENERAL COUNSEL, AIR TRANSPORT ASSOCIATION OF AMERICA, WASHINGTON, DC

Mr. LANDRY. Thank you, Mr. Chairman.

My name is James Landry. I am senior vice president and general counsel of Air Transport Association of America, which represents most of the scheduled airlines of the United States.

Our member carriers collectively operate over 97 percent of the revenue passenger miles, and about the same percentage of the freight miles flown in this country by the scheduled airlines.

We are pleased to have this opportunity to discuss with you the effects of airline deregulation on the rural economy, not only because of the critical role that economy plays in determining the economic health of the nation as a whole, but also because an evaluation of those particularized effects is an essential factor in the overall assessment of the bold statutory and policy changes which were overwhelmingly adopted by the Congress in the Airline Deregulation Act 9 years ago.

In my prepared statement, I set forth in some detail our overall assessment of deregulation, as measured against the express intent of Congress set forth in section 102 of that act. I do that because of the intensity of the spotlight which Congress and the media have focused on that assessment during the past several months.

I strongly believe that if you make your own objective appraisal of the results versus the intent, you too will come up with a positive scorecard. Yes, there has been turbulence and disruption, as many of the original proponents of deregulation predicted there would be, but the most visible symptoms—an upsurge of airline flight delays and a parallel upsurge of consumer complaints about the quality of airline service in general, both of which began to appear in 1986—have not only halted but turned dramatically downward since midsummer due in large part to remedial measures taken by Government and industry alike.

In the last half of my prepared statement, I discuss the more particularized focus of this hearing—the effect of deregulation on the rural economy. Here too, we believe the assessment should be positive. As this subcommittee is acutely aware, fears that freedom of entry and exist portended a wholesale abandonment of airline service to small communities prompted Congress to include in the 1978 act the provisions establishing the Essential Air Service Program.

That EAS Program guaranteed that any community served or authorized to be served by a certificated carrier on the date of enactment would be provided, through subsidies if necessary, an appropriate level of service for 10 years.

Mr. Chairman, we believe the EAS Program has worked well. It has entailed only a modest amount of Federal subsidy when compared to its predecessor, subsidized local service in the regulated era. More importantly, according to a comprehensive Brookings Institution study of the economic effects of deregulation, the only communities which completely lost air service in the first 5 years

of deregulation, 95 in number, were those not served by certificated carriers—thus, communities which would be equally exposed to abandonment in a regulated environment.

The Brookings study also opined that such communities were likely candidates for renewed service as equipment and pilots became available. And, of particular relevance to this hearing, the analysis further concluded that travelers originating at each hub classification, including the non-hubs—the category in which small communities fall—had reaped a welfare gain from deregulation.

Under the EAS guarantee, service to the great majority of small communities, those which had been certificated for service prior to 1978, not only continues today but is demonstrably improved. True, many of these communities have seen jet service replaced by small propeller-driven aircraft. But the smaller planes have offered many more departures and, by virtue of hub-and-spoke operations, many more destinations.

From the perspective of the rural economy this translates into greatly enhanced air service for short haul, predominantly business travelers to and from small communities. I am pleased to say that the member carriers of ATA, in recognition of the contributions the EAS Program have made to the continued pervasiveness of the national air transportation system and to the economic well-being of the both rural America and the nation as a whole, fully support the extension of that program sought in measures now pending before both houses of Congress.

In other words, Mr. Chairman, when you took the interruption, I think you were doing God's work. [Laughter.]

As I described in some detail in my prepared statement, two major developments under deregulation are primarily responsible for what has been, we believe, an improvement in air service to small communities—the heavy emphasis on hub-and-spoke route structures and the burgeoning operations of the commuter airline industry.

The contrast between the sparse, inconveniently timed, multi-stop service by out-sized jet aircraft to a small handful of destinations which was available to these communities in the days of regulation and the frequent, convenient, connecting or nonstop service to dozens of destinations by properly-sized—often propeller-driven—aircraft today is clear and undisputable.

In sum, by the measures of departure frequency, schedule convenience, flight time from the local small community airports to connections at major airports, and numbers of destinations realistically available for speedy round trip business travel, small community service since deregulation has indeed improved.

I particularly invite the Members of this Subcommittee to consider the personal anecdote included in my prepared statement, for decertification—not service improvement—was often the option chosen in the regulatory area.

Before closing, I would like to offer a few thoughts on one of the additional issues the chairmen raised in their letter of invitation to testify here this morning—the contention made by some that rural communities are being forced to tolerate a disproportionate number of flight delays.

Our analysis of the industry's flight delay experience clearly shows that the delays are concentrated at the gates, and taxiing in and out, and flying to or from the major airports of the Nation.

It is the congested, busy JFK's, O'Hares, and the like which bear the brunt of the delays. To the extent that rural communities experience delays in their service, it is a domino effect emanating from those hubs.

That problem will not be cured, Mr. Chairman, without major and essential changes in the approach to managing and funding the chronically inadequate infrastructure of our national air transportation system—the airports and airways whose capacity has not kept pace with the demand unleashed by economic deregulation.

If Congress does not make major changes in the historic approach to managing and funding that infrastructure, changes to assure that funding, procurement and personnel management procedures and policies are fully and swiftly responsive to demand, the full benefits of deregulation will never be realized over the long term.

That, Mr. Chairman, is a task that the Congress should take on as quickly as possible.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Landry follows:]

STATEMENT OF
JAMES E. LANDRY
SENIOR VICE PRESIDENT AND GENERAL COUNSEL
OF THE AIR TRANSPORTATION ASSOCIATION OF AMERICA
BEFORE THE SUBCOMMITTEE ON THE RURAL ECONOMY AND FAMILY FARM
OF THE SENATE COMMITTEE ON SMALL BUSINESS CONCERNING
THE EFFECT OF AIRLINE DEREGULATION ON THE RURAL ECONOMY
OCTOBER 28, 1987

My name is James E. Landry. I am Senior Vice President and General Counsel of the Air Transport Association of America, which represents most of the scheduled airlines of the United States. Our member carriers collectively operate over 97 percent of the revenue passenger miles, and about the same percentage of the freight miles flown in this country by the scheduled airlines.

We are pleased to have this opportunity to discuss with you the effects of airline deregulation on the rural economy, not only because of the critical role that economy plays in determining the economic health of the nation as a whole, but also because an evaluation of those particularized effects is an essential factor in an overall assessment of the bold statutory and policy changes which were overwhelmingly adopted by the Congress in the Airline Deregulation Act nine years ago.

Because of the intensity of the spotlight which Congress and the media have focussed on that assessment during the past

several months. I would like first to refresh this Committee's recollection of what the Congress broadly and forcefully intended in that Act, and demonstrate to you what has been achieved. To do that, I propose that we reexamine the Declaration of Policy, Section 102 of the Airline Deregulation Act of 1978, which sets forth the original Congressional intent.

In that policy statement, Congress first asserted that safety was to be accorded the highest priority in air commerce and that every feasible safeguard should be adopted to prevent any deterioration in established safety procedures.

Next, the policy declaration called for a variety of adequate, economic, efficient and low-price services by air carriers and foreign air carriers.

As its fundamental change, the Congress also mandated the placement of maximum reliance on competitive market forces and on actual and potential competition to provide the needed air transportation system. Amplifying this thought, the new Section 102 called for the encouragement, development and maintenance of an air transportation system relying on actual and potential competition to provide efficiency, innovation, and low prices, and to determine the variety, quality, and price of air transportation services.

The Congress also ordered that unreasonable industry concentration, excessive market domination, and monopoly power be avoided. In furtherance of that objective, Section 102 called for the encouragement of entry into air transportation markets by new air carriers as well as the encouragement of entry into additional air transportation markets by existing air carriers.

The bottom line of all this was that the airlines were to become, in effect, a vehicle of mass transportation.

How has the experience measured up against those objectives? Have we become a vehicle of mass transportation? The answer is "yes." The airlines have become a major growth industry in our country; we have enjoyed a tremendous growth spurt in passenger traffic -- ten percent per year for the last two years. Our annual traffic has zoomed from a level of 275 million passengers in 1978 to a level of 418 million passengers in 1986, and we have set new traffic records for four consecutive years.

According to the latest Gallup survey, 54 million adults -- 32 percent of our adult population -- took airline trips in 1986. That far surpassed the previous record of 48 million or 28 percent in 1985. Seventy-two percent of adult Americans now have flown at least once in their lifetime. Fifty-four percent

of the trips taken in 1986 were for pleasure purposes, 46 percent for business purposes. The average air traveler in our country made 3.2 round-trips last year. I think you will agree that we have indeed become a vehicle of mass transportation.

A variety of adequate services? The U.S. airlines are operating 6.4 million flights annually -- over 17,500 flights per day. They carry over 1.1 million passengers per day. If you average that out, one of our aircraft now takes off every 4.9 seconds with a load of 65 passengers bound directly for their chosen destinations or for highly sophisticated, connecting flight patterns offered at our industry's strategically placed hubs. So, there has been a great deal more service triggered by deregulation.

Low prices? We estimate that there were more than $3 billion in savings for our domestic passengers last year, as compared to the previous year alone, because of the widespread discount fares. Ninety percent of our airline passengers used some form of reduced fares in 1986, and the average depth of the discount was about 60 percent. This year, the comparable figures through August were about 92 percent and 62 percent, respectively. And the average airfare dropped 7.8 percent last year, the largest drop ever. Surely, there can be little argument over the fact that the price is lower for the great majority of air travelers.

But that is only part of the story, from the consumers' viewpoint. The Brookings Institution (Brookings) has concluded that deregulation has meant an annual savings for consumers of $5.7 billion, as measured in 1977 dollars. If you translate that into 1986 dollars, that comes to almost $10.3 billion in annual savings for consumers. Of that, Brookings concluded that one-third, or over $3 billion is attributable to fares (as ATA has also estimated), but the other two-thirds, almost $7 billion flows from the consumers' savings resulting from service improvements -- the combined effect of frequencies and travel time in the hub-and-spoke era, as contrasted to the old days of linear route operations.

How about the Congressional objective of encouraging new entries? There we have a mixed bag. In the first years after deregulation, there was a tremendous blossoming of newly certificated carriers, but in recent months, there has been a return to a level of concentration rather similar to that which existed before deregulation. But Congress intended not only to encourage entry into air transportation markets by new air carriers, it also encouraged the entry into additional air transportation markets by existing air carriers -- and, on the latter score, the proliferation continues. Yes, a mixed bag as I said, but there can be no question that deregulation in the United States has spawned the world's most competitive air transport industry.

How about safety? Has it suffered? While some of the critics would have you believe it has, if you take a look at the record, we submit that the answer is that it has not. The tragic accident at Detroit, so fresh in all our minds, tends to obscure the fact that the major U.S. airlines operated for 23 months without a fatal accident. Before Detroit, over 11 million flights were operated without a fatal accident -- truly remarkable, but not surprising in view of the dedication of airlines and government alike to maintaining safety as the highest priority in air commerce.

In summary, then, an overall assessment of deregulation, as measured against the express intent of Congress, must be positive. But I am not here to suggest that there has not been turbulence and disruption, as many of the original proponents of deregulation predicted there would be. Beginning in 1986 and continuing until mid-summer of this year, there was an upsurge of airline flight delays and a parallel upsurge of consumer complaints about the quality of airline service in general. These developments triggered remedial measures by government and industry alike.

Regulations have been drafted, debated and finalized by the DOT and, by and large, accepted by the airlines as necessary steps at this time; unfortunately, we can not say the same about some major features of legislation now pending here in Congress.

For our part, the airlines have individually and collectively adjusted their schedules, and worked cooperatively with the FAA to improve operating procedures. And airlines individually, as a clear reflection of the marketplace at work, have been reacting vigorously to the complaints of the customers. The results are highly promising; since mid-summer the FAA and the DOT have consistently reported dramatic drops in flight delays and consumer complaints.

I want to stress that those improvements have been made despite the chronic inadequacies of the infra-structure -- airports and airways whose capacity has not kept pace with the demand unleashed by economic deregulation. If Congress does not make major changes in the historic approach to managing and funding that infrastructure -- changes to assure that funding, procurement and personnel management procedures and policies are fully and swiftly responsive to demand, the full benefits of deregulation will never be realized over the long term. We would urge this Subcommittee to do everything in its power to see to it that such fundamental changes are given serious consideration by the Congress and, as soon as practicable, brought into effect.

Let me turn now from that overall assessment of deregulation, both as to the past and the future, and discuss the more particularized focus of this hearing -- its effect on

the rural economy. In response to fears that freedom of entry and exit portended a wholesale abandonment of airline service to small communities, the 1978 Act included an express safeguard against such a serious deterioration of the national air transportation system. Any community served or authorized to be served by a certificated carrier on the date of enactment was guaranteed, through subsidies if necessary, an appropriate level of service for ten years.

That Essential Air Service (EAS) program, which has entailed only a modest amount of federal subsidy when compared to its predecessor, (subsidized "local service") in the regulated era, has worked well. According to a comprehensive Brookings study of the economic effects of deregulation, the only communities which completely lost air service in the first five years of deregulation, 95 in number, were those not served by certificated carriers -- thus communities which would be equally exposed to abandonment in a regulated environment. The Brookings study also opined that such communities were likely candidates for renewed service as equipment and pilots became available. The analysis further concluded that travelers originating at <u>each</u> hub classification, including the "nonhubs" (the category in which small communities fall), had reaped a welfare gain from deregulation.

Under the EAS guarantee, service to the great majority of small communities, those which had been certificated for

service prior to 1978, not only continues today but is demonstrably improved. True, many of these communities have seen jet service replaced by small propeller-driven aircraft. But the smaller planes have offered many more departures and, by virtue of hub-and-spoke operations, many more destinations. From the perspective of the rural economy this translates into greatly enhanced air service for short-haul, predominantly business travelers to and from small communities.

In their very well-researched and well-reasoned new book, "Deregulation and the Future of intercity Passenger Travel", (at p. 15), Professor John Meyer of Harvard and Professor Clinton Oster, Jr. of Indiana University summarized: "Most pre-deregulation concerns about possible adverse social impacts also do not seem to have materialized. By most measures service to small communities is now at least as good, and probably better, than under regulation and the subsidy cost to the government is dramatically lower. But a few communities have lost service, and in some instances all service."

Two major developments under deregulation are primarily responsible for what has been, we believe, an improvement in air service to small communities. First, the intense competitive climate has prompted virtually every carrier to realign its route structure, with primary emphasis on hub-and-spoke operations. Secondly, the concentration of major

airlines upon medium to large markets has stimulated heightened activity by commuter carriers in the smaller markets. Moreover, there has been a healthy interplay between the two developments -- the burgeoning commuter airline industry is responsible for operating many of the essential spokes throughout the system.

In recognition of the efficiencies and cost savings involved, the evolution of the nation's airline route map from the historic linear route concept to predominantly hub-and-spoke carrier networks has been resolute and relatively swift, aided in several instances by mergers. The ramifications for small communities have been many-fold. Meyer and Oster describe air service to the more remote parts of the country and to small communities in the days of regulation as follows: "the CAB had evolved a program of local service subsidies that induced airlines (by the time of deregulation primarily local service airlines and not the trunks) to provide service to small communities; by the mid-1970s most of this service was performed in jet aircraft not particularly well suited to such activity ... Commuter carriers with more suitably sized equipment were not eligible to receive pre-deregulation small community subsidies. Before deregulation local service airlines typically used their jets in multi-stop service from one small community to another during late evening or midafternoon hours with the main

economic incentive being the collection of a government subsidy; this also kept these jets available for more remunerative service in higher-density markets elsewhere during the peak business hours."

The concern that these jets would naturally be assigned to denser, profitable markets in the deregulated environment, leaving the small communities with little or no service, prompted Congress to introduce the EAS program, which the member airlines of ATA fully support. The winners, I submit, are the residents and the economies of the historically under-served small communities.

The commuters, because they operate smaller, less costly aircraft, can afford more frequent flights in small markets than the local service carriers provided with their out-sized jet aircraft, routinely far less than half-filled with revenue passengers. Moreover, with economic passenger loads boarding their small, properly sized aircraft at many communities, the commuters are able to offer direct, non-stop service to hub airports, rather than the multi-stop flights previously offered by local service carriers. When one considers that analyses of DOT traffic data by both Brookings and Boeing have revealed that approximately 92% of all true origin and destination domestic traffic involves travel to or from a large hub, convenience and importance of these more frequent, non-stop

flights for business travelers from small communities is readily apparent.

Perhaps a personal anecdote would tell the story best. Almost thirty years ago, I started my career as a young route attorney with the CAB. At that time, under considerable pressure from Congress and the then Bureau of the Budget, the Board was doing its best to reduce the annual subsidy bill for service to small communities. We were all busy enforcing a "use-it-or-lose-it" policy, which meant that any community which did not board at least five passengers per day on a subsidized carrier's services (usually two flights per day) was to be wiped off the nation's airline route map forthwith. In a field hearing at one of those small towns in South Carolina, a battery of witnesses -- the mayor, the chief executive of a textile mill, the president of the Chamber of Commerce -- told us that, if they had a non-stop flight to Atlanta between 7 and 9 a.m. and a return flight between 5 and 7 p.m., they would use it. But what they had was useless -- a multi-stop flight to Atlanta late in the morning and a multi-stop return late in the evening. In the God-like roles we played at the Board, we chortled that every community wanted those business-hour non-stops, but it just wasn't feasible for all of them to have it, and we expunged the town from the route map.

Mr. Chairman, those community leaders were crying out for a hub-and-spoke complex and we didn't know it. They were crying out for the life-blood that regular, convenient air service brings to a community's economy and we ignored them. I know that today that town is not listed in the Official Airline Guide; I'll never know how many other textile mills never moved there or how many other businesses or factories never considered locating there because they couldn't engage in air commerce. What a pity that we didn't have hub-and-spoke networks nation-wide at that time! What a pity that we didn't have nation-wide service by hosts of commuter carriers, sometimes subsidized, with properly sized propeller-driven aircraft! That, in a nutshell, is what deregulation has meant to the economy of rural America.

Meyer and Oster concluded that, by the measures of departure frequency, schedule convenience, and flight time from the local small community airports to connections at major hubs, small community service since deregulation has generally improved, although not by as much as has service to larger communities. Based on my own experience in the old CAB route cases, I would add to those measurements one more virtue of the hub-and-spoke concept -- the passenger boarding at one of those communities years ago had four or five possible destinations for travel within a 24-hour day, as determined by the identity of the points along the linear route; today, he or she has two

or three dozen destinations fanning out in convenient connecting flights available at the hub.

Before closing, I would like to offer a few thoughts on one of the additional issues the Chairmen raised in their letter of invitation to testify here this morning -- the contention made by some that rural communities are being forced to tolerate a disproportionate number of flight delays. Our analysis of the industry's flight delay experience clearly shows that the delays are concentrated at the gates, and taxing in and out, and flying to or from the major airports of the nation. It is the congested, busy JFK's, O'Hare's and the like which bear the brunt of the delays. To the extent that rural communities experience delays in their service, it is a domino effect emanating from those hubs. That problem will not be cured, Mr. Chairman, without a major and essential change in the approach to managing and funding the infrastructure of our national air transportation system. And that, Mr. Chairman, is a task that the Congress should take on as quickly as possible.

The CHAIRMAN. Gentlemen, as I mentioned earlier, I am aware of one country's tourist bureau refusing to schedule service for their tourists to areas being served by commuter airlines. What is your reaction to that fact? Let me just ask Mr. Coleman.

Mr. COLEMAN. I am not really sure that I understand your question.

The CHAIRMAN. Somebody must think that there is a lack of sufficient service to communities served by commuter airlines.

Mr. COLEMAN. The United States is so completely different, I think, from most other——

The CHAIRMAN. There are people who will fly, and like to fly, and want to visit America. These people will even tolerate some delays to get where they are going. But when it comes to being forced to fly on commuter planes, these same people say no. They will not visit areas with commuter service. Does that not say something to you?

Mr. COLEMAN. It does say to me that this is a problem that is, I think, is faced by the transportation network of this Country. I do see some things, I think that over time, are positive signs, primarily the increasing number of working relationships between commuter airlines and major carriers, that I think over time is already beginning to lead to more sophisticated inner-line working arrangements; inner-line ticketing, inner-line baggage arrangements up through fares. These things, over the long pull, will be positive steps toward getting more remote areas of the United States back onto the airline map.

The CHAIRMAN. Is it your feeling that essential air service is one of these positive developments?

Mr. COLEMAN. Certainly the Department has taken the position that in those areas where essential air service has been the reason that communities remain on an airline map, those that in fact have markets measured in terms of price—will continue to get air service.

The CHAIRMAN. It is my understanding that the Administration opposes the continuation of EAS.

Mr. COLEMAN. That is correct.

The CHAIRMAN. So, it does oppose the continuation of EAS?

Mr. COLEMAN. That is correct. The Administration has taken the position that the essential air service program has——

The CHAIRMAN. How does the elimination of EAS improve rural air service?

Mr. COLEMAN. I think that our position would be that it does not materially affect it one way or the other.

The CHAIRMAN. What if the result is that there would be no air service to a good number of communities in America. It is clear that many communities would be abandoned with the elimination of EAS. Do you deny this? Do you think that if EAS is discontinued that all the communities presently being served by EAS will continue to have air service?

Mr. COLEMAN. No, sir. Our analysis is that there are probably about 70 communities that are now subsidized that would probably lose their air service.

The CHAIRMAN. Does that enhance, and provide better air service to those 70 communities?

Mr. COLEMAN. It does not. But by putting it in context these are communities that generate very little air traffic even with subsidized air service.

The CHAIRMAN. Let me ask another question. Does the DOT have the same quantity and quality of information that the CAB had with respect to the number of passengers and airline miles, fares, and so forth?

Mr. COLEMAN. In some respects, we did have the same and in some other respects we did not. Let me explain that. One of the reasons for that is that there is now so much more participation by the commuter air carrier industry. There never was a provision, for example, in our origin and destination survey. There never was any provision for us to be able to capture all of the data where a commuter airline was carrying all the traffic.

The CHAIRMAN. How does the DOT know? How is the DOT in a position to know what the effects of airline deregulation actually are? How can DOT make the assertion that the service is getting better if the DOT does not have the information to know this?

Mr. COLEMAN. We do have data. We do have data reported directly to us from those carriers that we were subsidizing.

The CHAIRMAN. In many cases, you have less information?

Mr. COLEMAN. We also have information, Mr. Chairman, to the flow of traffic. For example, if a passenger enplanes at an airline in a small community and let us say goes to Chicago and then connects to a major airline and goes to Los Angeles, unless that journey is written on a single ticket we will only capture the Chicago to Los Angeles portion of his journey. The commuter portion of it will not be reported in the origin and destination our survey.

It has always been that way. The reason that I say that that is more important now is because the commuter airline industry is participating a lot more in carrying traffic.

The CHAIRMAN. Let me ask a more general question. Is the failure of jet service in some of these communities due to the lack of equipment; is it due to insufficient incentives to develop the equipment; what is the reason?

I have a gut feeling that there could be enhanced service with different incentives. If not jet service, then some kind of comfortable turboprop equipment with sufficient baggage space. Do you agree that rural communities would be provided with better equipment if incentives were there?

Mr. FREDERICKSEN. I do, Mr. Chairman. I think that you are absolutely right. If the incentives were there, as I mentioned, every member of my association would buy a bigger airplane. The incentives are passengers getting on the airplane and buying tickets.

I pointed out in my prepared statement an example in Redmond, OR, where the people there lost jet service. They decided that they were going to take a dramatic step to get it back. What they did was get corporate pledges to put into an escrow account to guarantee an airline a certain number of passengers per day and if the airline did not get those passengers they could dip into the escrow account. They did get direct jet service to San Francisco with that method. It is an economic incentive.

The CHAIRMAN. Let us address the question of national responsibility, and national obligations. I mentioned earlier this morning

that all of us have helped to foot the bill for the DC Metro System. I must say that it is $6 billion, and 80 percent of that, to my understanding, is taxpayers money and 20 percent of it is fares. We all pay for the Metro System. It was a good thing for Washington, DC. But I will tell you, most of us would probably rather not live in Washington, DC, but in other parts of the country.

Second, the entire country is provided with an Interstate Highway System; and a postal system. One can think of all kinds of examples where all taxpayers are paying for service in the urban areas.

So, why should not the same principals be applied to air service? Do any of you have any thoughts about that?

Mr. LANDRY. Well, I might offer one, Mr. Chairman, that Congress overwhelmingly obviously made a decision back in 1978——

The CHAIRMAN. I am not talking about what Congress did, I am talking about the policy. What is right here? Can you think of any logical reason why the urban taxpayers should help build highways, interstate highways in sparsely populated parts of the country but not help provide for air service in sparsely populated parts of the country.

I do not care if Congress did or not. I am interested in policy here.

Mr. LANDRY. The pressures, it seems to me, continue today to avoid an increase in Federal Government subsidy of those services. I think there is a very serious philosophical, moral question which Congress does have to face there. But I think there are only two options for attracting the kind of service that you spoke of—improved service or jet service to some of the smaller communities.

Either the increase in traffic that Mr. Fredericksen spoke of, or an increase in Federal subsidy, or State and local subsidization, which was also contemplated back in the Deregulation Act as a possible option for the future.

The CHAIRMAN. Let me ask a direct question. Is there any instance of robbing Peter to pay Paul here? That is, are there any cases where some rural passengers are helping to pay for service to urban areas?

Mr. COLEMAN. Mr. Chairman, if I may address that.

The CHAIRMAN. One has to ask that question. There are discount fares, to high density urban markets, the $99 coast-to-coast fares, and so forth. Yet, we all know—let us be honest with ourselves—that rural areas do not get those discounts. Fares do not go down, they go up. I know DOT has some figures on fares that show otherwise, but I must say, Mr. Coleman, they remind me of the tyranny of averages, the draining of averages.

I am addressing the problem of rural America, where it is obvious that the fares certainly have not enjoyed the same reduced fares as the high density urban markets.

Mr. FREDERICKSEN. Mr. Chairman, although most of our carriers—43 out of the top 50—are in some sort of marketing relationship with a major carrier, the vast majority of the regional airlines are independent companies. The companies that you see operating service between the smaller communities in the major hubs are not the same companies that are operating the long distance jet air service.

In most cases there is not that opportunity to rob Peter to pay Paul, because Peter and Paul are two separate entities. With a few exceptions, that is generally the case.

The CHAIRMAN. Does anyone else have a view on that subject? Mr. Coleman.

Mr. COLEMAN. I was going to raise that. What I regard as a related matter on the issue of robbing Peter to pay Paul, if you look at the transportation system as involving the north, there have been situations where we have been contacted by service transportation operators who have complained that by our subsidizing air service between a small community and a hub we are diverting from the surface transportation operations that are going on of valuable traffic. To some extent, that is a perverse result.

The CHAIRMAN. Therefore, you agree with Mr. Dempsey's suggestion that we set up a separate, independent regulatory agency that regulates all forms of transportation? You must agree with that proposal then?

Mr. COLEMAN. No, sir. My point was that there is—I do not have a view on that, Mr. Chairman. (Laughter.)

My point was that in looking at the philosophy—is it in the public interest for us to continue to subsidize air transportation in isolation to small communities, I think it is important for us also to look at the effect that that has on other modes of transportation that are not being subsidized.

If we look at the issue of cross-subsidization, I think that that is an important consideration.

Mr. CADWELL. Mr. Chairman, on the issue of cross-subsidy, the one side effect of the deregulation, of course, has been the increase in small airline service companies. Mr. Fredericksen has said that to the extent that any of those small companies have lower entry costs, essentially, smaller aircraft, your capital startup costs are not that great.

So to the extent that any one of them were charging significantly more than it was costing them to operate, they would find, I think, it easier than it would be to serve a major market where you have to acquire landing slots and where you have to acquire large aircraft. The new entrants essentially serves to keep the monopoly rent, as the economists would say, from being charged.

Mr. LANDRY. If I could add another thought, Mr. Chairman. The $99 fares that you alluded to are virtually entirely capacity controlled fares, a product of this new science of yield management. They are available only for a limited number of seats. Their whole objective is to fill those empty seats on the large jet aircraft with pleasure travelers, leisure travelers.

That is a marketing science that has developed since deregulation.

The CHAIRMAN. Why does not Eastern Airlines do the same thing for rural areas? How about $9 to fly from Montana to Denver? They would fill up those planes pretty quickly.

Mr. LANDRY. I believe the load factors in Mr. Fredericksen's numbers are comparably high.

The CHAIRMAN. Charge $90 and still fill them up.

Mr. FREDERICKSEN. You have to have 30 passengers paying $150 to have the other 6 pay $9.

The CHAIRMAN. It is obvious that those $99 fares are made up somewhere. As far as various—you just cannot do it.

Mr. LANDRY. I think, Mr. Chairman, and I do not want to beat it to death. If the marketing people of his members conclude that they can get greater revenues and minimize the number of unused seats by doing that, they will do it.

The CHAIRMAN. What about safety? Do you have adequate safety statistics, Mr. Coleman, to know whether a smaller airlines safety record is as good as Mr. Fredericksen thinks it is?

Mr. COLEMAN. The information that we have seen does support that view.

The CHAIRMAN. The information you have seen? That is not the question I asked. The question I asked is if you have adequate information?

Mr. COLEMAN. I believe we do, sir, yes.

The CHAIRMAN. Is that the same information that is available to——

Mr. COLEMAN. Yes, sir.

The CHAIRMAN. For regulation?

Mr. COLEMAN. Yes. In addition to that, with regard to the Essential Air Service Program, I might say that we have added an additional element doing what we call "reliability inspections" so that if a new air carrier is embarking for the first time when serving an essential air service market, we look very closely at that carrier on site, in order to ensure that they are prepared to perform reliably as well as safely.

The CHAIRMAN. Mr. Fredericksen, as you heard earlier, Mr. Schofield said that a recent survey of Furtune 500 firms decided that they would not locate plants and facilities in certain areas that do not have adequate airline services.

I can tell you that Montana has experienced this very problem. We in Montana, have tried over the last 6 or 8 months to encourage U.S. West to locate a research facility in Montana. One of the first questions U.S. West asked was about the availability of adequate airline service.

We did not get the U.S. West facility. I have a hunch that the reason is, in part, because of insufficient airline service.

People talk about air service and business investment being a Catch 22. It really is not a Catch 22 situation. Airlines must first provide the service to get the passengers. They can't wait for the passengers to come to them.

Why have not the smaller airlines made a much greater effort to provide better service; what is the reason?

Mr. FREDERICKSEN. First of all, Mr. Chairman, you have to understand where we are coming from. We would love to provide more enhanced air service to these communities. That is what we are in business to do. The bigger the airplane, the more money that we would make.

We would certainly, every one of our members, would love to do that. Running a small airline, Mr. Chairman, is a very, very expensive endeavor. Frankly, most of our companies simply cannot afford to put in startup service and leave it for say, 6 months, hoping that service can be generated while a new industry comes

in and then wait for the traffic to develop. We simply cannot afford to do that.

You cannot afford to fly airplanes empty. It is probably one of the most cash-intensive sort of endeavors that you can get into. So, our marketing people, just the same with any other business, find the markets where we can make the money.

Now, there is always some effort, both through advertising and through startup service, and you will see carriers a lot—start service into markets hoping that they generate better traffic by having the service there. And, you will see them pull back when it turns out that they simply just cannot afford to do that.

The CHAIRMAN. I have other questions that evolve around the same point, and I do not want to beat this to death either. I will just solve it by saying that I think there is a real problem here and we have to find a solution.

I do not know what the exact solution is, but I do know we need better air service to less-populated areas of our country. This has to be done.

Looking for that solution, I have introduced a bill calling for a bipartisan, blue ribbon commission to study the effects of airline deregulation. The Commission would study its effect on both urban and rural America. We need to study the effects of airline deregulation, preserve its benefits, and find solutions for the problems it causes.

I thank you all very much. This will not be the last time that we will visit this subject, I am sure. You have all been very patient, and I apologize again for the delays this morning.

I thank you very much for coming.

[Whereupon, at 12:30 p.m., the hearing adjourned.]

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